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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

UNITED STATES OF AMERICA, EX
REL. ALEX GRABCHESKI,

Plaintiff,

v.

10 CV 3902 (GBD)

AMERICAN INTERNATIONAL GROUP,
INC.,

Defendant.

New York, N.Y.
July 22, 2015
11:00 a.m.

Before:

HON. GEORGE B. DANIELS

District Judge

APPEARANCES

BUTZEL LONG, P.C.

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F7M9USAA

(In open court; case called)

THE COURT: Good morning. Why don't I hear from you first, Mr. Burck, on your motion.

MR. BURCK: Thank you, your Honor.

I wanted to start with a procedural question that's a little bit unclear to us at the moment because of essentially how the relator has responded to our motion to dismiss.

THE COURT: I would address the third amended complaint.

If that's your question.

MR. BURCK: For the record, your Honor, I think that they've conceded that the second amended complaint should be dismissed and if that's the case we'd like that on the record so we can then address this essentially as our opposition to the motion to file the third amended complaint.

THE COURT: However they want to respond to it but I consider the third amended complaint to have superseded the second amended complaint. So if I do not allow the amendment I'm going to dismiss the case unless somehow the third amended complaint is different. Somehow the claim is that the second amended complaint is sufficient in a way that the third amended complaint isn't.

MR. BURCK: Thank you, your Honor.

THE COURT: Did you want to respond?

MR. GOLDFARB: Your Honor, I think that's right. I

F7M9USAA

1 don't have anything additional to say about the second amended
2 complaint that wouldn't apply to the third. So I think if we
3 lose on the third we're certainly not going to win on the
4 second.

5 MR. BURCK: Thank you, your Honor. What I'll do then
6 your Honor, I will address our opposition to the third amended
7 complaint.

8 Your Honor to start with the threshold matter that we
9 actually haven't briefed because we learned of this in
10 response -- after the relator filed their opposition to our
11 opposition to their motion to amend. And that has to do with
12 the specific language of 31 U.S.C. Section 3730, which is the
13 key provision for the False Claims Act here, (B)(4)(b). And
14 that provision, your Honor, says that the relator, "Must have
15 voluntarily provided the information to the government before
16 filing an action under this section."

17 At the time -- and I think the relator doesn't contest
18 this -- at the time this statute was jurisdictional. The
19 language was jurisdictional. It has changed because of the
20 Obama care statute made it more flexible. But at the time it
21 was jurisdictional. Again, it said that the relator must have
22 voluntarily provided the information to the government before
23 filing an action under this section.

24 Now the relator admits in their briefing that the
25 disclosure here took place after their action was commenced.

F7M9USAA

1 The relator's original complaint was filed on May 12, 2010 and
2 the relator, by his own admission, first provided information
3 about this case to the government in June of 2010, so about a
4 month later.

5 Again this is a jurisdictional issue at the time that
6 the provision that applies in this case. The relator basically
7 tries to glide by this in the brief by asserting that he
8 provided the information to the government before he originally
9 asserted the specific claim at issue, which is the alleged
10 falsity of AIG's representations in the debt reduction
11 agreements; that it was the claim that was filed after they
12 provided the information to the government. But, your Honor,
13 the clear, plain language of the statute is that it's an
14 action, when the action is filed. Not when a claim is
15 presented in an action.

16 So, your Honor, there is doesn't seem to be any way
17 for the relator to get around that particular jurisdictional
18 bar. They simply essentially defaulted in a sense because they
19 provided -- they filed their complaint, their original
20 complaint, before they actually provided information to the
21 government. And there is no -- they provide no case law, no
22 statutory provision, nothing to refute that or suggest that
23 there's something we're missing.

24 So, your Honor, as a threshold matter we think this
25 case needs to be dismissed because at the very outset it was

F7M9USAA

1 faulty. We didn't know that until literally a few weeks ago
2 because, of course, this was all under unseal. They had no
3 obligation to provide that information to us until they
4 responded. So that is, as a threshold matter, your Honor, this
5 case should be dismissed.

6 THE COURT: You haven't addressed that in any of your
7 submissions.

8 MR. BURCK: We have not, your Honor. We have not had
9 an opportunity to do that because we learned it as a result of
10 the last set of briefing. We are happy to do so and it may, in
11 fact, be worthwhile to do so, of course, your Honor, but that
12 seems to us to be a pretty strict hurdle they cannot overcome.

13 THE COURT: Why don't you -- on that issue why don't
14 you submit me a letter on that issue and they can respond by
15 letter.

16 MR. BURCK: Yes, your Honor. We'll do that.

17 THE COURT: You can submit a letter in ten days.

18 MR. BURCK: Yes, your Honor.

19 THE COURT: Before the end of the month, on the
20 31st. And they can respond by the 10th of August.

21 MR. GOLDFARB: Yes, your Honor.

22 MR. BURCK: Thank you, your Honor.

23 I'll turn to the merits now of the third amended
24 complaint. Before I do that I just want to talk a little bit
25 about the context. The relator talks a bit about the context,

F7M9USAA

1 but I think there's a little bit more that should be explained
2 about the context of this whole case that has been going on for
3 a long time so you have an understanding of how this all plays
4 out when we get to the merits.

5 Now the heart of the relator's action is that AIG's
6 former subsidiaries, ALICO and AIA, conducted supposedly an
7 illegal insurance business in various states, including
8 New York, and that AIG's statements to the U.S. Government that
9 ALICO and AIA were in full compliance with state laws were
10 false statements.

11 The relator claims that the alleged false statements
12 are in these debt reduction agreements between AIG and the
13 Federal Reserve, which basically used ALICO and AIA as a kind
14 of ownership interest, the federal government got an ownership
15 interest in those entities, sort of collateral on the loan that
16 AIG got as part of the financial crisis.

17 So this is actually a very unusual False Claims Act
18 case because we have an alleged federal violation that is
19 premised on an alleged state law violation, which is itself
20 premised on business activities of former AIG subsidiaries
21 whose business activities had nothing to do with federal law
22 and the federal government. These were state-regulated
23 insurance businesses.

24 So the alleged fraud in this case is purely derivative
25 of a supposed state law violation. And reflecting this sort of

F7M9USAA

1 odd setup the relator has essentially pursued two tracks in his
2 efforts to bring this case to court.

3 The federal track began about five years ago, a little
4 over five years ago where the relator filed the original
5 complaint and provided the U.S. Government with information
6 about ALICO and AIA in around June 2010. And then the civil
7 division of the U.S. Attorney's Office for the Southern
8 District of New York as well as the SIG TARP, which was the
9 Special Inspector General for the TARP program, which was
10 active at the time, investigated the relator's claims.

11 And as the court is aware, the Southern District of
12 New York declined to intervene in this case back in October of
13 2013, so a little under two years ago.

14 Now at the time that the Southern District declined,
15 relator's first amended complaint was pending. And the first
16 amended complaint was prepared about two years before Southern
17 District declined, around June of 2011. It was filed in July
18 of 2011. All under seal.

19 That's significant for a couple reasons, your Honor,
20 in terms of when we get to the merits. It's important to know
21 that before the relator went to the Southern District of
22 New York in his original complaint he made no mention at all --
23 and he concedes this -- of this supposed unlicensed insurance
24 business as being a basis for his claim, his federal False
25 Claims Act claim. No mention of it at all.

F7M9USAA

1 The Southern District started investigating this case
2 right after -- and started looking into that issue, the issue
3 that we have here today, in 2010. Again, the complaint didn't
4 mention it. The Southern District started looking into it
5 nonetheless.

6 It was a year later that the relator then had the
7 first amended complaint which then offered up this theory which
8 has now evolved into the current third -- proposed third
9 amended complaint.

10 Your Honor, the reason why I mention this in
11 particular is because the relator wants the court to take a
12 look at the declarations to add substance to the third amended
13 complaint to understand more about the original source concept,
14 the public disclosure concept.

15 Well, we think that the court -- we invite the court
16 to take a very close look because what's interesting about what
17 they have put in the declarations is they never, ever say where
18 they got this theory from, this theory they have now. They
19 never say that they gave it to the Southern District of
20 New York.

21 They say they gave the theory to the DFS, the DA's
22 Office -- the Department of Financial Services, the DA's
23 Office, the AG's Office. Those are all, of course, state
24 institutions, state governed.

25 They never say that they gave it to the Southern

F7M9USAA

1 District of New York. I think that's important, your Honor,
2 because the inference is very clear that they didn't give it to
3 the Southern District of New York. They probably got it from
4 the Southern District of New York.

5 And again, your Honor, I think it's fair for us to
6 reference this because they want the court to take a close look
7 at those declarations, outside the four corners of the
8 complaint, to make a determination about the substance of their
9 complaint. And I think it is very clear, your Honor, that they
10 must have gotten this theory from the Southern District of
11 New York.

12 Just a few other background issues and I'll get to the
13 substance, your Honor.

14 Now the Southern District of New York's declination
15 shouldn't have surprised anybody because the federal
16 government, led by the Federal Reserve and the Treasury
17 Department, as most people know, lived inside of AIG for years
18 following the financial crisis.

19 The debt reduction agreements, which were later
20 claims, contained the false statements, were negotiated,
21 diligenced and executed by the federal government with hordes
22 of lawyers, bankers, accountants, and everybody else,
23 diligencing these deals.

24 So, when the Southern District eventually declined
25 that really shouldn't have been much of a surprise. But what

F7M9USAA

1 relator then did is they went to the state -- again, this is
2 all from the basis of their briefs and their declarations --
3 they went to the state and they asked the state, the DFS, the
4 DA's Office, the AG, to look into this issue. And that did
5 lead to consequences for MetLife, which purchased ALICO and AIA
6 from AIG, and also for AIG. It was state law consequences and
7 state settlements.

8 As the Court knows, MetLife settled with the DFS on
9 March 31 of 2014. They signed a consent order. And in that
10 consent order, which was only between MetLife and DFS, AIG is
11 alleged by DFS to have violated certain New York insurance laws
12 at the time it owned ALICO and this company called GMD which
13 was the marketing entity that worked with ALICO to market its
14 products.

15 So based on that allegation in the consent order that
16 MetLife signed with DFS, AIG sued DFS in federal court, in
17 front of Judge Nathan. And we raised arguments about the
18 constitutionality of the statute, if it was read to -- if it
19 was interpreted to mean what DFS seemed to suggest it meant.
20 And we raised arguments about statutory provisions. And we
21 fully briefed it in front of Judge Nathan on a motion to
22 dismiss basis. And then we settled the case with DFS.

23 So there was never an adjudication of that issue. But
24 that was the framework. And, again, the reason why that's
25 important is because you're going to understand, your Honor,

F7M9USAA

1 where a lot of their theories come from in this third amended
2 complaint.

3 So we had at this point, before they filed their third
4 or they proposed their third amended complaint, we have a DFS
5 consent order with MetLife that says that MetLife committed
6 various violations after it owned ALICO and GMD. We have AIG's
7 consent order. We have also a DA's Office DPA, deferred
8 prosecution agreement, with MetLife; not with AIG. And we have
9 AIG's briefing on all of these issues related to the New York
10 state law, constitutional issues, how it would implicate
11 federal law. That's the context in which the relator then
12 created this proposed third amended complaint.

13 The relator has belatedly tried to fix what are
14 essentially conceded with the glaring deficiencies in the
15 second amended complaint by borrowing, cutting and pasting,
16 from all of the things I just mentioned; consent orders, even
17 from AIG's briefing and complaint against DFS in terms of how
18 we characterize the activities that happened. And they do that
19 because, of course, the second amended complaint, they
20 essentially acknowledge, is deficient. But this of can't work
21 to save the relator's claims for a bunch of reasons.

22 First, your Honor -- again, this is all, of course,
23 briefed and I will try to be as brief as I can be in addressing
24 some of these issues. But on the public disclosure bar which
25 is of course part of 31 U.S.C. Section 3730. Again, it was a

F7M9USAA

1 jurisdictional issue at the time. It compels dismissal where
2 the relator cannot meet his burden to show beyond a
3 preponderance of the evidence that the information on which the
4 allegation of fraud rests was not a public disclosure and the
5 relator's allegations are not based on or substantially similar
6 to a public disclosure.

7 Now taking up this public disclosure issue first. Of
8 course, there's also alternatively the original source issue.
9 I'm going to look at the public disclosure first and then I'll
10 address the original source.

11 Now, on the public disclosure issue, ALICO's New York
12 based marketing and sales activities, and it's Delaware based
13 underwriting activities, which are the core of the claims, were
14 disclosed in various AIG press releases and reports and
15 including occasionally even in regulatory reports long before
16 the federal -- the crisis occurred long before the DRAs came
17 into effect long before Mr. Grabcheski came up with his
18 complaint.

19 And we've cited to and quoted from in our brief a
20 number of these instances in which this is actually disclosed.
21 I'm just going to read from one, your Honor. It's in 2008. So
22 again this is before the financial crisis, long before all the
23 issues we have here today.

24 In that press release, on March 2008 AIG said: AIG
25 group management division -- which is GMD, which is the heart

F7M9USAA

1 of the issue in this case -- is a division of the life
2 insurance subsidiaries of AIG. Headquartered in New York, GMD
3 operates in more than a hundred countries. GMD's employee
4 benefits, credit insurance, and global pension products and
5 services are offered through the various life insurance
6 subsidiaries of AIG including AIA and ALICO.

7 Your Honor, the relator wants to say well, that
8 doesn't tell us that GMD actually operated from New York. Well
9 what it says is that GMD is headquartered in New York and what
10 it does is it markets insurance products for ALICO and AIA to
11 multinational corporations. The gravamen of their claim is
12 that GMD, from New York, had people working here who were
13 marketing ALICO's products to multinational corporations. It
14 actually doesn't matter for their theory whether or not the
15 multinational corporations are in the United States or
16 overseas. What matters is that there was somebody here in
17 New York doing it. That's theory. Your Honor, that is the
18 case right there. That's the underlying activity. And it was
19 disclosed in March of 2008.

20 And then we cite a bunch of other press releases and
21 other reports that buttress this. And in context, if you read
22 them all, it could not be clearer that the idea that GMD -- it
23 was not known to the public that GMD was doing this from
24 New York, it just doesn't withstand scrutiny.

25 Your Honor, again, I won't belabor the point because

F7M9USAA

1 we quote from a bunch of different sources in the brief. But I
2 think it will be a hundred percent clear.

3 I'll just briefly touch on the underwriting, the
4 secret underwriting, as the relator mentions, in Delaware.

5 The secret underwriting was actually documented in the
6 Delaware Insurance Department's administrative reports. In
7 fact, the Delaware insurance regulator was concerned about
8 layoffs at ALICO and GMD in Delaware because it would affect
9 underwriting business in Delaware.

10 So, again, the idea that the regulator didn't know
11 about it simply doesn't make any sense because they are worried
12 about people losing their jobs who are doing underwriting in
13 Delaware.

14 Now, the third amended complaint, the proposed third
15 amended complaint actually worsens the situation for the
16 relator than the second amended complaint, in our view, because
17 it literally cuts and pastes from the very definition of a
18 public disclosure, which are the consent orders, our briefs,
19 and the Manhattan D.A.'s Office's deferred prosecution
20 agreement.

21 And it does that because it needs particularity. It's
22 trying to meet -- they're trying to meet Iqbal and Twombly.
23 They try and do that by literally taking language -- most often
24 not even similar language, not paraphrasing; literally taking
25 the language and sticking it in their complaint.

F7M9USAA

1 As I said, these are the very definition of public
2 disclosures. And nothing in them that make specific claims
3 about specific activities that allegedly violated specific
4 New York laws, none of these specific issues that are put out
5 in the consent order, that are now in the third amended
6 complaint, ever made their way into any prior complaint by the
7 relator. Ever.

8 The relator, finally, got a roadmap for their theory
9 from the DFS consent order. That's why the third amended
10 complaint is here. That's why they've abandoned the second
11 amended complaint.

12 The case law is clear. The relator cannot evade the
13 public disclosure bar by filing -- by having filed three
14 defective complaints over the course of four years, and then
15 file a fourth that copies and pastes from further public
16 disclosures. That's not the way the law works. The entire
17 case is drawn now from public disclosures.

18 Now, the relator initially -- I'm turning to the
19 original source issue, your Honor. The relator initially, in
20 his first brief, discounted the original source theory and said
21 we don't need that, we don't need to worry about that. But
22 then after our opposition, they then try to put some meat on
23 the bones and they want the court to look at the declaration
24 and the exhibits to the declaration in order to say that
25 Mr. Grabcheski was the original source for all of these claims

F7M9USAA

1 for the unlicensed insurance.

2 Of course, your Honor, we already know that he wasn't
3 the original source in the original complaint. We know that.
4 They concede that.

5 We also know that the Southern District of New York --
6 well, your Honor, I will stipulate that we don't know this but
7 I would invite counsel to address it -- we know that the
8 Southern District of New York investigated that issue before
9 Mr. Grabcheski put it in his first amended complaint. So, we
10 know that he's not an original source in that sense.

11 What does he say he's an original source about? He
12 says he has direct and independent knowledge of the underlying
13 claim in this case. That's the statutory requirement.

14 I want to break that down for a minute because there's
15 really three necessary but distinct aspects of this claim. One
16 is that he had to have direct and independent knowledge of the
17 underlying marketing activities of ALICO and GMD and AIA.
18 That's one concept. Two, he had to have independent and direct
19 knowledge of the state insurance laws that were allegedly
20 violated by these activities. And three, he had to know that
21 the debt reduction agreements that contained the allegedly
22 false statements, he had to know about those as well. Those
23 are the way that you get to the federal False Claims Act case.
24 Any one of these alone is not sufficient, without the others,
25 to establish the relator as an original source of the

F7M9USAA

1 information that gave rise to this case. This is so because
2 only together do they give rise to a potential violation of
3 federal law.

4 Consider this, your Honor. The underlying activities
5 have no bearing -- the underlying activities themselves have no
6 bearing or relevance to any federal issue unless they give rise
7 to a state law violation, which in turn must breach some
8 federal obligation. Here purportedly the allegedly false
9 statements in the DRAs that ALICO and AIA were compliant with
10 state laws. That's the only way we're here. The underlying
11 activities themselves mean nothing without everything else. So
12 in isolation none of these give rise to even a hint of a
13 federal claim under the federal False Claims Act.

14 And there's nothing in the pleadings contained in the
15 original complaint, the first amended complaint, or the second
16 amended complaint that articulate with any particularity or
17 specificity at all the claim that now appears for the very
18 first time in the third amended complaint and is lifted,
19 shamelessly, one must say, from the most public disclosures,
20 the consent orders and the DFS, and the other public
21 disclosures that I referenced earlier.

22 Now seeking to amend the complaint for a third time to
23 us is a tacit admission of this fact by the relator himself.
24 Now he realizes that the prior complaints failed on Iqbal and
25 Twombly and now tries to resurrect this action by claiming, in

F7M9USAA

1 the most conclusionary fashion, and again without any
2 specificity at all in the third amended complaint, that he was
3 the original source of the claims embodied in DFS's consent
4 orders.

5 Now, to be sure, the relator has submitted
6 declarations attempting to establish that he's an original
7 source. But none of these allegations about the relator's and
8 his counsel's disclosures is actually found in the third
9 amended complaint itself. You have to look in the declarations
10 and the side -- and the other documents that are outside of the
11 complaint to start to understand the explanation as to where
12 this -- how this was originally sourced to Mr. Grabcheski.

13 Now it does make you wonder if there's going to be a
14 fourth amended complaint in order to try to bring some of that
15 in. But right now it's not in the third amended complaint.

16 Even more of a problem is that, as seen in the
17 relator's own declaration, relator actually has no direct and
18 independent personal knowledge of either the alleged underlying
19 insurance activities. He concedes he learned that from other
20 people. He was a human resources official or executive. He
21 was not doing the sales and marketing. He learned about it
22 from others who worked with him.

23 And he also didn't know anyone at AIG who was
24 specifically involved in the negotiation and execution of the
25 debt reduction agreements which are the basis for this claim.

F7M9USAA

1 He didn't know anything about any alleged misrepresentations
2 because he wasn't even at AIG when the DRAs were drafted,
3 signed, executed. He was gone. He had been fired.

4 THE COURT: Well I'm not sure I fully understood the
5 extent of your argument on original source. Is your argument
6 that he can't be an original source if someone in the company
7 disclosed to him the illegal activity?

8 MR. BURCK: Your Honor, our position is -- not quite
9 that far, your Honor.

10 THE COURT: All right.

11 MR. BURCK: Our position is -- and we base this off
12 of, for example, U.S. Rosner v. Stellar IP Owner LLC, which we
13 cite in the brief. It's not that he can't -- that he can't
14 learn of activities that are illegal and then disclose them,
15 become a whistleblower in that sense.

16 The issue is that his knowledge of these activities
17 are purely derivative of what other people have told him. He
18 wasn't participating in any way in any of these activities.

19 THE COURT: I'm not sure there's a requirement that he
20 has to be a participant in the activities in order to qualify.

21 MR. BURCK: Your Honor, fair point. I think the issue
22 here is that it has to be more -- again, we rely here on the
23 cases that we cited in the brief, that it shouldn't be -- the
24 law is not that somebody who happens to be around the company
25 who happens to be -- who hears about something, especially --

F7M9USAA

1 especially, your Honor, in the context of the disclosures that
2 had already occurred by AIG, that that makes you an original
3 source under the law.

4 THE COURT: But if someone in the company, a fellow
5 employee in the company, discloses illegal activity in the
6 company to him and that activity is not publicly disclosed. He
7 is now, other than the person who disclosed the activity to
8 him, he's the only person that knows of this activity. You're
9 saying he can't qualify as the original source if he discloses
10 that he was given this information by another employee in the
11 company to the U.S. Government.

12 MR. BURCK: Your Honor, let me do this. I'm going to
13 quote from the Rosner case which is interpreting Second Circuit
14 law on this issue. And what the Second Circuit -- again this
15 is in the Rosner case, has interpreted the Second Circuit to
16 mean, and I'm quoting. The Second Circuit has interpreted the,
17 quote, direct and independent knowledge requirement to bar
18 suits where a third party, not the relator, is the source of
19 the core information upon which the qui tam complaint was
20 based.

21 And in that case, in the Rosner case, the judge
22 decided the relator was not the original source where he
23 learned of the alleged misconduct by interviewing other people.

24 THE COURT: No. I understand that. I understand that
25 rule.

F7M9USAA

1 I'm not sure if that's what you're arguing here. Are
2 you arguing that as an employee of the company, that if another
3 employee discloses to him illegal activity, that he can't be
4 the original source of that information if he gives that
5 information to the government?

6 MR. BURCK: Your Honor, I don't think it has to be as
7 broad. It's not a categorical bar, your Honor. Not at all.

8 I think in the circumstances here, given several
9 factors, your Honor, given the fact that AIG had already
10 disclosed GMD's activities and ALICO's activities.

11 THE COURT: That's a different issue. That's public
12 disclosure. I'm not addressing that issue now. You separated
13 the two issues, and I'm just addressing right now the issue of
14 whether or not he can be an original source.

15 You say regardless of the public disclosure,
16 independent of the public disclosure issue, he cannot qualify
17 as an original source because the information came from where?

18 MR. BURCK: Well, your Honor, in this case the
19 information came from the fact that he happened to be working
20 at GMD and observed and learned from many other people,
21 including the public disclosures, your Honor -- that's how I
22 was bringing it in, as the original source -- about these
23 activities that were going on at GMD openly.

24 And on top of that, your Honor -- and, again, this is
25 why it's a circumstance. I'm not making a broad argument

F7M9USAA

1 that --

2 THE COURT: That's a public disclosure argument.
3 That's not an original source argument.

4 MR. BURCK: I think the issue is that when it comes to
5 the original source -- this is why I mentioned the fact that in
6 the original complaint where Mr. Grabcheski came to the
7 government or filed under seal and then came to the government
8 with a bunch of claims about what was going on at AIG and at
9 ALICO and GMD, he didn't include this one. He did not include
10 the one that he's pursuing now.

11 THE COURT: As I review your original source argument,
12 you don't want me to conclude that he can't -- that a person
13 can't -- does not qualify as original source --

14 MR. BURCK: No, your Honor. We're not --

15 THE COURT: -- if someone says to them -- if a
16 vice-president says to him, while he's working there, at the
17 watercooler, you know what, I just came out of a meeting and
18 they just decided they're going to go and defraud the
19 government and take money from the government. You're not
20 saying that he can't take that information, give it to the
21 government, and qualify as the original source of that
22 information if that information is not otherwise publicly
23 disclosed.

24 MR. BURCK: No, your Honor. Absolutely. We're not
25 taking that position. We're not looking for a bright line rule

F7M9USAA

1 about whether or not a whistleblower -- what constitutes a
2 whistleblower in the context of an original source.

3 THE COURT: You're saying he's not an original source
4 because it was publicly disclosed or he's not an original
5 source because of where the information came -- where the
6 private information came from?

7 MR. BURCK: Your Honor, we're saying he's not an
8 original source because of where the information came from to
9 the government and in a sense that his -- the idea that
10 Mr. Grabcheski is the original source, again, for the three
11 aspects of this case, it's not him.

12 THE COURT: But would you -- if the information did
13 not come to the government from a third party and if the
14 information wasn't already publicly disclosed, is there any
15 argument that he cannot qualify as an original source?

16 MR. BURCK: Your Honor, I think that it's --

17 THE COURT: Are those tied together?

18 MR. BURCK: Your Honor, I don't believe -- we're
19 certainly not making that argument. I think that the Second
20 Circuit and the rule -- it's obviously still somewhat open or
21 unclear. We're not making that argument, your Honor.

22 We're being very specific about Mr. Grabcheski. So we
23 don't need to say: Well, everything else fails and therefore
24 what happened here was that he just got it from other people.

25 THE COURT: So your primary argument is that the

F7M9USAA

1 government -- the government did not get this information
2 originally from him.

3 MR. BURCK: That's right, your Honor. That's part of
4 the argument.

5 Then just to go back to what we're saying about
6 Mr. Grabcheski. And I think this goes to the heart of the
7 court's question about the bright line about who -- who was the
8 original source, who isn't, do you have to be, can you just
9 overhear it at the watercooler?

10 Your Honor, I think that the hypotheticals that you're
11 posing are very different than what happened in this case, and
12 this is why we're talking the circumstance of this case. If
13 Mr. Grabcheski learned of secret information, like we're going
14 to go defraud the federal government, from a third party at the
15 company, I think there's very little doubt that that person is
16 a whistleblower.

17 Here our argument is -- this is why I mentioned the
18 public disclosure -- he learned of publicly known information,
19 or information that was being provided to the government
20 through other people, including subpoenas to AIG and ALICO and
21 MetLife; that that's how the government learned -- the
22 government being the Southern District of New York. DFS, and
23 with all respect to DFS and the D.A.'s Office, are not
24 obviously relevant in the sense of the federal False Claims Act
25 issues here; that he learned about it from public sources and

F7M9USAA

1 that's what we think is abundantly clear from even his own
2 declarations.

3 Just to be very specific, your Honor. When I say that
4 he learned about this while he was working at human resources,
5 my point is that the information he learned at human resources,
6 amongst all the people at GMD, was public information. It
7 wasn't: We're going to go defraud the federal government. It
8 was literally, Judge: My job is to be a sales and marketer for
9 GMD for ALICO. That's what I do. That was my title. And he
10 then goes and says: Guess what, government, we have people who
11 are doing sales and marketing in New York. And that's not
12 secret information, your Honor. That was publicly known
13 information. So on that, just on the underlying activities
14 alone he's not getting secret information. He's recycling
15 public information.

16 Then when we go to the next two steps it becomes even
17 more clear that he's not the original source of the arguments.
18 The state law violation. Your Honor, he wasn't even able to
19 articulate the state laws that were violated until DFS put it
20 on a consent order. And then he put it into his third amended
21 complaint.

22 The second amended complaint, your Honor, actually
23 postdates the MetLife consent order by about a month, and also
24 our arguments in front of Judge Nathan. And yet even in the
25 second amended complaint he didn't put in those arguments. I

F7M9USAA

1 don't know why, but he didn't. He did it now, a year later.
2 It's self-evident that it didn't come from him. And, again,
3 this is a strange case where the legal issue is actually part
4 and parcel and a necessary piece of the federal claim. Because
5 it has to be a state law violation in order to hit the third
6 element, which is the debt reduction agreement. And that, your
7 Honor, that really he has no -- he doesn't even really make an
8 argument that I can discern as to how he's the original source
9 of that.

10 The debt reduction agreement was a public document, of
11 course. It was signed by the federal government and AIG and
12 ALICO and AIA. And he has no basis, none -- he doesn't even
13 say he learned about it from somebody, that the representations
14 in it, which are the basis for the federal claim, were false.
15 So, he fails more dramatically at each level, but he fails at
16 each level. And that's why we don't think he's an original
17 source.

18 Your Honor, I'm going to turn to a couple of other
19 issues and this deals with the falsity of the statements and
20 the knowledge -- the knowledge requirement for the falsity.

21 Now as I mentioned, of course, this is essentially a
22 derivative claim of the DFS consent orders. It's essentially
23 just repeating what they've said.

24 Now, the allegations became public as a result of the
25 consent orders. The allegations in this case, which, again,

F7M9USAA

1 are the underlying activities violate state law and, therefore,
2 AIG violated federal law, became public as a result of the
3 consent orders. And we cannot ignore that fact when we assess
4 the third amended complaint.

5 Now, none of the relator's authorities that he cites
6 for the third amended complaint's viability support the
7 assertion that allegations from a consent order can remain in a
8 complaint under the circumstances here where the allegations
9 became public because of the consent order. In other words,
10 the law is clear that the consent order -- a consent order
11 shouldn't be cited for any purpose. And in the consent order
12 itself for DFS, between DFS and AIG and DFS and MetLife, it's
13 abundantly clear that it's only about a settlement between the
14 parties. There are explicit statements that it cannot be used
15 for other purposes.

16 Of course, for AIG's consent order there was no
17 adjudication at all. This was simply a finding by DFS. No
18 adjudication. And the law is very clear that that's not
19 something that should be used in any kind of complaint. And,
20 again, the allegation was made public by the consent order.

21 Under those circumstances, we have not found a case
22 that says that you can use the consent order in your complaint.
23 And therefore, the consent order, which is the basis for the
24 particularity in the third amended complaint, should be
25 stricken. And if you strike all of that, the cut and paste

F7M9USAA

1 from the consent orders, then you're back to the second amended
2 complaint. And the second amended complaint, which relator
3 appears to concede is at least -- is deficient under Iqbal and
4 Twombly.

5 THE COURT: I'm not sure why it technically needs to
6 be stricken. Because your argument, even if it's in there,
7 it's not sufficient for a factual allegation demonstrating the
8 original source of nonpublic information.

9 MR. BURCK: That's right, your Honor. In fact, I only
10 mention this because in the event that we are not successful on
11 the first argument that I think that this part -- and I think
12 also on -- and I'll explain this in a moment -- I think even
13 with respect to the falsity statement, the reason why I mention
14 the striking is because if you get to the point where you
15 actually look at the falsity, the falsity has to be premised --
16 is premised on the consent order, the consent order saying that
17 AIG -- a finding that AIG violated New York state law by the
18 DFS. Once you take that out, which it seems under the case law
19 you'd have to, then there's nothing left under the second
20 amended complaint. You don't have to get there. But that's
21 why we're addressing that.

22 I'll skip ahead to the knowledge portion because this
23 is why we don't think it ultimately really should matter for
24 purposes of striking the consent order provisions that are in
25 the third amended complaint.

F7M9USAA

1 On the knowledge -- the False Claims Act, of course,
2 requires knowledge; some level of knowledge, reckless
3 disregard, willful blindness, or actual knowledge.

4 Here, the case law is very clear that the issue is:
5 Was AIG's understanding of the law unreasonable? We cite the
6 case from Judge Chin, Colucci, and other cases, Taylor v.
7 Gabelli, that make it very clear that you've got to look at the
8 unreasonableness. If you're basing it on a legal principle to
9 get to your False Claims Act case, you've got to look at the
10 unreasonableness of the interpretation.

11 Your Honor, in this case -- I'm not going to go into
12 it, your Honor, because I don't think this is necessarily ripe
13 for you to hear right now, unless you're interested. We don't
14 think that AIG's view of the law was unreasonable at all. In
15 fact, AIG sued DFS in federal court to assert that, in fact,
16 the law, as interpreted by DFS, was wrong. We settled the
17 case. But there was no -- there was never any adjudication as
18 to the issue of whether or not we were right or DFS was right.
19 That has been left unsaid.

20 Now the unreasonable issue here really turns on
21 whether or not the law, as DFS has interpreted it, is correctly
22 interpreted. And our view is that it isn't. And we go into
23 some detail in the brief. Again, if the Court wants me to go
24 through that I can. It's basically -- the argument is that the
25 statute itself does not apply to these types of activities on

F7M9USAA

1 its face. And if they do, then they create constitutional
2 issues for the statute. And that was --

3 THE COURT: I'm not sure that's even an appropriate
4 inquiry on this motion.

5 MR. BURCK: Exactly, your Honor. That's why I'm not
6 going to go into it. That's one of the reasons why the
7 unreasonableness -- the only way I think it comes into play,
8 your Honor, is the question of whether on its face the position
9 that AIG has taken for many years and argued in front of Judge
10 Nathan was unreasonable.

11 The broader or the bigger problem with the knowledge
12 element, as alleged by Mr. Grabcheski, really goes to this
13 collective knowledge point, which is that Mr. Grabcheski cannot
14 identify and has not identified a single person with any
15 specificity, not a single human being at AIG or ALICO who knew
16 both about the underlying activities that were going on at
17 ALICO and who also signed or was involved in the negotiation or
18 knew about the misrepresentations alleged by Mr. Grabcheski in
19 the debt reduction agreement. He lists ten people whom he says
20 are people who knew.

21 Well, your Honor, five of them left AIG before the
22 debt reduction agreement was signed. So I'm not sure what the
23 relevance of those people is. Then the other five, most of
24 them are ALICO employees. Four of them I believe are ALICO
25 employees, who had nothing -- he doesn't even allege they had

F7M9USAA

1 anything to do with the debt reduction agreement or had any
2 role in negotiating for AIG or signing anything for AIG with
3 the federal government.

4 Then he has one person who signed one of the debt
5 reduction agreement contracts. But he doesn't allege, because
6 he can't, with any specificity, that that person knew anything
7 about ALICO -- about ALICO's underlying activities or knew
8 there was a violation of state law. There's literally not a
9 single human being, which of course is required by law, to
10 allow the respondeat superior to go up to the corporation.
11 There's not a single person that Mr. Grabcheski has identified
12 who knew that: A. what was going on at ALICO and GMD violated
13 state law; and B. nonetheless negotiated, participated in, knew
14 about, agreed to, signed the debt reduction agreement. So
15 without that you cannot have a collective -- if he wants to
16 piece it all together and say various people had different
17 pieces of knowledge and that carries up to the corporation.
18 Your Honor, that's clearly not the law. There is no basis and
19 any case law to suggest that he can do that.

20 Just briefly, your Honor. He also claims, he tries to
21 bring in a bunch of other states beyond New York to say well,
22 we violated this law and that law and this law and that law
23 doing these things. Well, your Honor, it's plain as day, and
24 in not only the complaint but also in the briefs, that there's
25 literally no specificity at all as to what we even did, what

F7M9USAA

1 he's saying we did in those states and what laws or provisions
2 of what laws we specifically violated.

3 The reason for that, your Honor, we believe is because
4 he didn't get a roadmap from those regulators. New York did
5 investigate and did have settlements with MetLife and with AIG
6 and gave him a roadmap for how to put this together. But those
7 other states didn't do that. So he doesn't know. So he just
8 puts in undifferentiated claims that we did things like we did
9 in New York and other states. That's literally what he says,
10 more or less. And then he has block quotes of statutory
11 provisions that it's completely unclear on their face how they
12 have anything to do with the activities that are at issue. He
13 certainly doesn't try to explain it.

14 So, your Honor, with respect to the knowledge and the
15 of falsity there's just no -- there is no claim, there's
16 nothing he's alleged in even the third amended complaint that
17 gets you anywhere close to getting falsity. Now we don't think
18 we need to get there because we think he fails public
19 disclosure, original source, etc. But if we do, that is
20 clearly a barrier that he can't overcome and he hasn't overcome
21 after four attempts.

22 Last topic. I'll be very brief on this topic. This
23 is materiality. This is only if they manage to get through all
24 of the other hurdles. The materiality point, your Honor,
25 really comes down to Mr. Grabcheski claims that the loss amount

F7M9USAA

1 here to the government was about a hundred million dollars.
2 Now, how does he get there? He gets there by counting up the
3 settlement numbers from the consent orders by DFS, the state
4 entity. Now, he doesn't explain or doesn't claim to know how
5 those numbers came up or anything. And also, your Honor,
6 there's something a little odd about it, because AIG owned
7 ALICO and GMD for 50 years. MetLife owned them for about two
8 or three years. MetLife paid \$60 million. AIG paid \$35
9 million. So there's obviously something wrong with the
10 calculation if you're going to base it on that kind of
11 calculation. But he uses that to say it's a hundred million
12 dollar loss.

13 That is plainly insufficient. That doesn't even come
14 close under any standard. Forget Iqbal and Twombly, the prior
15 standard, to even meet a materiality threshold.

16 This was a humongous deal, \$24.4 billion dollars was
17 the value of the two companies combined, when they were put
18 into these special purpose vehicles and given ownership
19 interest by the U.S. government. The U.S. government forgave
20 \$25 billion worth of debt on this basis. The idea here is
21 something like well if it was a hundred million dollars less,
22 then the deal would have blown up. Well, your Honor, I think
23 that we all know that that wasn't what this deal was about.
24 And also certainly that doesn't make any sense, .5 percent of
25 the deal. But even that, your Honor, pales ultimately when you

F7M9USAA

1 look at what actually happened with this deal on the
2 materiality front. The U.S. government got paid back
3 everything they loaned to AIG. Every last dollar. And the
4 federal government has been very clear about that. The
5 Treasury has been very clear about that. There was a case in
6 D.C. that was well known when Mr. Greenberg sued the federal
7 government about this whole deal.

8 There is no question that the materiality aspect here,
9 if you have -- if you ever get there, is completely -- is
10 almost preposterous. So your Honor with that -- those are the
11 basic principles. Again, they sort of go, as the Court pointed
12 out, ratcheted down to materiality as the last hurdle for a
13 motion to dismiss purposes. But that is -- that is essentially
14 our argument, your Honor. If you have any questions, further
15 questions, I can answer those.

16 THE COURT: No.

17 Let's take a break first for the court reporter.

18 (Recess)

19 MR. GOLDFARB: I apologize, your Honor.

20 THE COURT: That's okay. I guess the heart of it
21 seems to me to be to define what information and in what way
22 that the plaintiff was the original source of what was at that
23 time nonpublic information, and was the original source and
24 provided that information to the government.

25 MR. GOLDFARB: Your Honor, the original source issue

F7M9USAA

1 doesn't even arise unless the Court first finds that the public
2 disclosure bar is triggered. We think that it was not
3 triggered here. So unless the Court makes that finding that it
4 was triggered, doesn't even have to get to the original source
5 issue.

6 THE COURT: My question is really more direct than
7 that. What's really pivotal to clearly define for me and
8 articulate what was that information. What was the public
9 information -- what was the nonpublic information that was
10 possessed by the plaintiff that he disclosed to the federal
11 government.

12 MR. GOLDFARB: Your Honor, the nonpublic information
13 was the facts that demonstrated that the representations in the
14 debt reduction agreement were false.

15 THE COURT: So what information was that?

16 MR. GOLDFARB: The information was that ALICO and AIA
17 were involved in insurance activities in New York and also
18 other states, but I think since the disclosures that AIG relies
19 on relate to New York, let's focus on that, but his
20 information -- and this was in the first amended complaint when
21 this claim was first asserted. The theory was that ALICO and
22 AIA were engaged in unlicensed insurance activity in New York.
23 That information had not been disclosed in the 2008 press
24 release at all, which Mr. Burck read, but he left out an
25 important piece of the language from that press release. He

F7M9USAA

1 said -- the press release said GMD is headquartered in
2 New York. And that of course doesn't mean they conduct
3 marketing activities. But the press release also said, and
4 it's quoted on page 20 of AIG's original memorandum, if you'll
5 excuse me. They quote -- the language of that 2008 press
6 release said: AIG group management division, GMD, is a
7 division of the life insurance subsidiaries of AIG.
8 Headquartered in New York, GMD operates in more than one
9 hundred companies. And then the part he left out was: Through
10 a regional and local management structure.

11 So what that 2008 press release did is it said it was
12 headquartered in New York. It did not say they're involved in
13 marketing or solicitation in New York. And did say that it
14 operates through a local and global management structure, which
15 creates the impression that it's all distributed all over the
16 world since they're selling insurance in other countries.

17 So that, far from disclosing that they're doing
18 insurance activity in New York, suggests the opposite; that
19 they're doing the insurance activities overseas in their
20 various regional and local offices.

21 So that does not at all disclose that they were
22 involved in marketing of insurance in New York, that they
23 needed to be licensed, that they weren't licensed. None of
24 those facts is disclosed. Of course, why would AIG announce in
25 a press release we're involved in an illegal insurance

F7M9USAA

1 activity. That makes --

2 THE COURT: I'm trying to focus on the actual factual
3 information.

4 MR. GOLDFARB: Yes.

5 THE COURT: This is not a securities fraud case. It's
6 not about whether or not the company had an obligation to
7 publicly disseminate information to investors so that they can
8 make investment decisions.

9 I'm trying to understand what is the -- it's unfair to
10 characterize it this way -- but what is the secret information
11 that your client had that the rest of the world -- no one else
12 in the world knew about except those people involved in that
13 illegal activity.

14 And I understand -- you're not saying that your client
15 was the source of information that these entities were involved
16 in insurance activity in New York. That was publicly known,
17 that they were involved in insurance activity in New York.

18 You say that the fact that they were involved in
19 unlicensed insurance activity in New York is the nature of the
20 information that you say was withheld from the government that
21 defrauded the government.

22 MR. GOLDFARB: Your Honor, the standard is not whether
23 this was secret information that was unknown out of AIG. That
24 is not the standard for public disclosure. For there to be a
25 public disclosure within the meaning of the False Claims Act it

F7M9USAA

1 has to be a disclosure through certain specified means; a
2 government report, the news media, etc. They're relying on the
3 press release as a news media disclosure. Those are all
4 they've come up with.

5 The fact that people -- the friends, the husbands and
6 wives of people who worked at AIG knew what those people did,
7 you know, in a colloquial sense, that's not secret certainly,
8 but that doesn't count for purposes of the False Claims Act.

9 THE COURT: But public disclosure is really
10 technically not the issue. The issue is whether or not the
11 information was disclosed to the federal government. That's
12 the only issue. We couldn't care less who else knew other than
13 the federal government. Because the crux of the claim is that
14 the federal government was defrauded. Because when they were
15 told they were in compliance with state laws, that they knew
16 that information was false, and they misled the federal
17 government into thinking that they were in compliance with
18 federal law when they really weren't.

19 So the question really is what is the specific
20 noncompliance information that was uniquely in the possession
21 of your client? That's what I need you to focus on.

22 MR. GOLDFARB: I'll tell the court what he disclosed
23 to the government and when he disclosed it. I don't think it
24 has to be uniquely in his knowledge. But in the first amended
25 complaint --

F7M9USAA

1 THE COURT: Well he's got to be the original source
2 for it.

3 MR. GOLDFARB: Right. But original source within the
4 specific technical definition which requires him to have
5 independent and direct knowledge of the information. And he
6 has to provide it to the government before filing an action
7 based on the information which, by the way, Mr. Burck made a
8 big deal of the fact that the information about the uninsured
9 insurance was not provided until after the lawsuit was
10 commenced. And that's true. But that doesn't matter. Because
11 what the statute says when it's defining original source, it
12 says you have to disclose it to the government before filing --
13 commencing an action that's based on the information. As
14 originally filed in this court, the first original complaint,
15 as Mr. Burck says accurately, did not include this complaint.
16 So at that time it was not an action that was based on the
17 information about the unlicensed insurance activity. It only
18 became an action based on that information when the first
19 amended complaint was filed.

20 In that complaint, in paragraphs 81 to 90 spells out
21 the activities that took place in New York that constituted the
22 unlicensed insurance activity.

23 THE COURT: Most of that information, your client
24 wasn't the original source of that information.

25 MR. GOLDFARB: Your Honor, he was.

F7M9USAA

1 THE COURT: In what way? Tell me what he found out
2 and how he found out.

3 MR. GOLDFARB: Yes. He was the director of human
4 resources administration. But to describe it as human
5 resources actually kind of gives the impression that his duties
6 were sort of more trivial than they were because we tend to
7 think of human resources as just part of the bureaucracy. But
8 he was -- I realize I'm going a little bit beyond the
9 complaint. But he was one of the -- the people who was
10 involved in -- sort of the brain trust within GMD.

11 THE COURT: So what information uniquely came to him
12 in that position.

13 MR. GOLDFARB: What he was able to find out about it
14 was through his duties -- for instance, he was involved in the
15 approval of incentive compensation payments for the sales
16 people who were working at GMD in New York; because of that,
17 was aware that the sales and the business they were getting
18 credit for was on behalf of ALICO and AIA, and it was for
19 business that was supposed -- it was being done in New York,
20 because the people who did it were based in New York. Through
21 that, through position descriptions, through that sort of thing
22 he was aware, as part of his duties, what these people were
23 doing. This was not just a watercooler conversation. He's
24 aware because of his duties what was going on.

25 He also was aware of the steps that were being taken

F7M9USAA

1 to try to conceal the activity such as putting employees who
2 were working for -- whose duties were for GMD and selling on
3 behalf of ALICO and who worked in New York, but they had to be
4 listed under the payroll of unrelated companies for whom they
5 really were doing nothing such as American General.

6 THE COURT: I'm not sure how I understand how it's
7 related to the unlicensed insurance in New York.

8 MR. GOLDFARB: Because that was to conceal -- by
9 putting them on those other companies, that created the
10 pretense that these people were not engaged in unlicensed
11 insurance activity.

12 For instance, the people from GMD were put initially
13 under American General, which was a licensed insurance company,
14 even though they did nothing for American General. And the
15 head of American General complained about it saying, What are
16 these people doing on my payroll? And he was told, We have to
17 put them there because they can't be on the AIG or ALICO
18 payroll because ALICO is not licensed to do business in
19 New York.

20 THE COURT: Who do you attribute that to?

21 MR. GOLDFARB: I'm sorry?

22 THE COURT: Who do you attribute that to? Who told
23 him that?

24 MR. GOLDFARB: Well --

25 THE COURT: You can't just say that's what I was told.

F7M9USAA

1 If that's specific information that he was provided, you have
2 to be able to tell me who gave him that information.

3 MR. GOLDFARB: Well, your Honor --

4 THE COURT: Is that in the complaint?

5 MR. GOLDFARB: The complaint does identify specific
6 high level AIG officers who were party to those discussions and
7 Mr. Grabcheski was involved with discussions and meetings where
8 this issue was discussed.

9 THE COURT: I know, but the way you just characterized
10 it is not a sufficient factual allegation. What I'm asking you
11 for is a specific factual allegation.

12 If you say -- I agree with you. It is much more
13 compelling if you say that your client was told by John Jones
14 at the company that the reason these people were put on the
15 payroll is because they had to cover up the unlicensed
16 insurance activity in New York. You've just represented to me
17 he had such a conversation with a person.

18 Who -- what are the circumstances of that conversation
19 and who provided him that information?

20 MR. GOLDFARB: Your Honor, one of the people was Ken
21 Nottingham who was the CEO of ALICO.

22 THE COURT: Said to him that the reason that they were
23 doing this was to cover up the illegal licensing activity?

24 MR. GOLDFARB: I think in substance. I don't think --
25 I'm not sure those were his words.

F7M9USAA

1 THE COURT: I assume those weren't his words. Those
2 are the words that you gave me. You said somebody told him
3 that it was done to cover up the unlicensed insurance activity.

4 Are you saying that your client can make an
5 affirmative representation in a complaint that a particular
6 individual, a responsible individual at AIG that he can
7 identify, said that to him?

8 MR. GOLDFARB: Well, your Honor, I can't -- I would
9 have to confer with Mr. Grabcheski.

10 I think the answer to that I can represent is yes.

11 THE COURT: That's not in this complaint. It's not in
12 any of the complaints.

13 MR. GOLDFARB: I don't think we need to do it in that
14 level of detail.

15 THE COURT: Well, you can't just say I was around and
16 I heard people say that this is what they wanted to do.

17 I mean I'm not even sure what -- why don't you give me
18 a couple of examples of specific factual allegations that you
19 say demonstrate his personal knowledge about illegal activity
20 at AIG. Just give me a paragraph or two.

21 MR. GOLDFARB: Your Honor, we discuss in the third
22 amended complaint, in fact, at paragraphs 104 to 126.

23 THE COURT: I'm sorry. I want to go to a paragraph
24 that you want me to rely upon so that I can say that this is a
25 factual allegation that your client came into possession of

F7M9USAA

1 information that illegal insurance activity was occurring and
2 tells me how he got that information and from whom he got that
3 information. Because that's the only way I can assess whether
4 or not it is publicly or nonpublicly disclosed information that
5 he is in possession of that he's now going to provide to the
6 government.

7 MR. GOLDFARB: Your Honor, I understand.

8 But, again, the question of public disclosure is not
9 whether in the abstract sense it's secret. The question of
10 public disclosure is has there been a disclosure through a
11 specified source. So you have to look at --

12 THE COURT: No. Whether or not -- I'm just
13 concentrating on the disclosure through your client. I'm
14 trying to figure out what information that you say your client
15 disclosed to the government that is the basis of this complaint
16 and where factually will I look to see, other than
17 conclusionary language, what exactly he got; what information
18 he got, how he got that information, so I can determine that he
19 was the source of that information and where does it say he was
20 the source of that information to the government. Give me an
21 example.

22 MR. GOLDFARB: Your Honor, if the Court will turn to,
23 starting at paragraph 104 of the third amended complaint.

24 THE COURT: 104?

25 MR. GOLDFARB: Yes.

F7M9USAA

1 THE COURT: Where does it tell me that he's receiving
2 information that he's going to subsequently pass to the
3 government?

4 MR. GOLDFARB: Your Honor, what these allegations
5 describe is the shuffling around of GMD personnel on the
6 payroll of various different AIG subsidiaries which
7 Mr. Grabcheski was involved in as the head of human relations
8 at GMD.

9 THE COURT: But it doesn't say that. It doesn't say
10 he has any relationship with this at all. Or even knew about
11 this at all. It just says it happened.

12 So I'm trying to figure out where do I look to say,
13 okay, this complaint gives me information that says that he
14 was -- provided this information and this information indicated
15 that they were making false statements to the government and
16 then he subsequently passed that information on to the
17 government. Because you would agree that that's what's
18 required.

19 MR. GOLDFARB: Well, your Honor, with respect, I don't
20 agree. Because I think the court is combining the public
21 disclosure issue with the original source issue.

22 THE COURT: Forget about public disclosure or original
23 source. I'm just trying to understand. You have a claim that
24 your client came into possession of certain information. I'm
25 trying to get you to articulate for me directly what

F7M9USAA

1 information you say that he came in possession of and how he
2 got that information and that he disclosed that information to
3 the government. Those are the three elements that you have to
4 meet. We can agree on that.

5 So, this paragraph does not tell me that he came into
6 possession of any information. This paragraph does not tell me
7 what information he came into possession of. And this
8 paragraph doesn't tell me that he disclosed that information to
9 the government.

10 It just says in general that AIG engaged in a series
11 of actions. But that's a conclusionary statement.

12 MR. GOLDFARB: You're right, your Honor.

13 THE COURT: What actions is he talking about and who
14 told -- how did he find that out and what did he do with that
15 information?

16 MR. GOLDFARB: Your Honor that paragraph was an
17 introduction to the paragraphs that follow. So that wasn't
18 intended to be the only statement.

19 THE COURT: So give me a line that tells me what
20 information that he came in possession of or give me a line
21 that tells me how he got that information.

22 MR. GOLDFARB: Your Honor, what he came into
23 possession of is all the information --

24 THE COURT: Where does it say that?

25 MR. GOLDFARB: It says that in his declaration.

F7M9USAA

1 THE COURT: I can't read his declaration. I'm reading
2 the complaint.

3 MR. GOLDFARB: Except, your Honor, I think for
4 purposes -- there's different -- there's a variety of different
5 issues here that have to be sorted out. For purposes of does
6 he adequately allege a fraud, I don't think he's required to
7 say in the complaint this is how I found it out. What we have
8 to do is give enough --

9 THE COURT: He's required to give me information,
10 enough factual information for me to determine that he had
11 information at the time before he filed this lawsuit and he
12 disclosed that information of this illegal activity to the
13 government.

14 MR. GOLDFARB: And that's something that can come in
15 outside the complaint. Because this goes to a jurisdictional
16 issue. We're allowed to put in evidence outside the complaint.

17 THE COURT: I'm sorry. Not to articulate your claim.
18 Your claim has got to be a plausible allegation in the
19 complaint. It can't be the complaint and I've got an affidavit
20 that's going to tell you how. I've got to look at the
21 complaint -- the four corners of the complaint have got to
22 conclude that this complaint sufficiently meets the elements of
23 this claim. And the elements of this claim are that he got
24 information that he gave -- and that information indicated to
25 him that there was illegal activity, and that illegal activity

F7M9USAA

1 was that the government was being defrauded, and he took that
2 information and he gave it to the government. That's got to be
3 in this complaint.

4 MR. GOLDFARB: Your Honor, with all respect, that's
5 not an element of the claim. That's an issue that relates
6 to --

7 THE COURT: Which is not an element?

8 MR. GOLDFARB: How he got the information. The fact
9 that he got the information. That's not an element that goes
10 to the liability for the False Claims Act.

11 THE COURT: But you have to be able to say that he got
12 the information because he doesn't have standing otherwise to
13 make this claim. You've got to tell me that -- I've got to
14 read this complaint and when I'm finished reading this
15 complaint I have to conclude that he had information that
16 indicated that AIG was involved in fraudulent activity. And he
17 gave that information to the government.

18 Right?

19 MR. GOLDFARB: Your Honor, that only becomes relevant
20 once there is an identification of a public disclosure through
21 a specified source. And there's -- we do allege in the
22 complaint there was no public disclosure.

23 THE COURT: Of what?

24 MR. GOLDFARB: Of the information in the complaint.

25 THE COURT: Of what information?

F7M9USAA

1 MR. GOLDFARB: Well we allege there was no public
2 disclosure.

3 THE COURT: Of what information?

4 MR. GOLDFARB: Well there was no public disclosure of
5 the information about the unlicensed insurance activity.

6 THE COURT: So you're saying that they did not
7 disclose to the government that they were involved in
8 unlicensed insurance activity?

9 MR. GOLDFARB: Correct.

10 THE COURT: What is -- how do I determine that --
11 let's go beyond the complaint. I'm going to stick with your
12 affidavit. Tell me what it is -- what is the unique knowledge
13 that he had of this?

14 MR. GOLDFARB: Your Honor, he had knowledge of the
15 unlicensed insurance activity. It doesn't have to be unique to
16 him. He does not have to be the only person who has that
17 knowledge.

18 THE COURT: Well he's got to be one of the people.

19 MR. GOLDFARB: Well, you're right.

20 THE COURT: And he's got to be somebody who knows when
21 most people don't.

22 MR. GOLDFARB: Well, your Honor, that's not --

23 THE COURT: Well that is true. That's a
24 whistleblower, you know it and most people don't, and you're
25 the one who discloses it.

F7M9USAA

1 MR. GOLDFARB: Certainly dealing with most people, I
2 think that's true.

3 THE COURT: That's in every case.

4 MR. GOLDFARB: You're right. That's true.

5 THE COURT: It's not like everybody knows. It's got
6 to be that he uniquely has some intimate knowledge of this that
7 he -- that he is now giving to the government; because the
8 government doesn't know about it, and it's not publicly known,
9 so the government wouldn't know about it. That's premise of
10 your claim.

11 MR. GOLDFARB: Although the question of whether the
12 federal government knows about it, that's not the test either.

13 THE COURT: No. It is the test on this factual
14 scenario you've given me because the nature of your fraud is
15 that they told the government that they were in compliance and
16 they knew they weren't in compliance. If you can't demonstrate
17 that, you have no case.

18 Right?

19 MR. GOLDFARB: Well if the government knew -- if
20 there's evidence that the government when they got the -- if
21 they -- when they got the debt reduction agreements.

22 THE COURT: Right. But the only false claim -- and I
23 can use "claim" in a generic sense -- the only false claim
24 you're alleging here is they claim they were in compliance with
25 state laws and you knew that they weren't in compliance with

F7M9USAA

1 state laws because they were doing unlicensed insurance
2 activity. That's the crux of the claim.

3 MR. GOLDFARB: Yes.

4 THE COURT: So the requirement is, and the sole focus
5 is: Was it true when they said that they were in compliance
6 with state laws, when they said that, did they know that it was
7 untrue or had reason to know that it was untrue, and that your
8 client had information that they disclosed to the government to
9 notify the government that they had been lied to.

10 MR. GOLDFARB: Yes.

11 THE COURT: I mean that's the essence. I mean I'm
12 breaking it down in its simplest terms.

13 MR. GOLDFARB: Your Honor, what was disclosed to the
14 government was -- initially was the first amended complaint.
15 And we've also submitted some other materials that were
16 disclosed to the government before the first amended complaint
17 was filed.

18 THE COURT: What information is that? Summarize that
19 information. That's what I'm trying to extract.

20 MR. GOLDFARB: One of the things we've identified is
21 the draft of the first amended complaint which we have not
22 submitted yet because -- frankly because the U.S. Attorney's
23 Office was concerned that by submitting a draft there would be
24 a waiver of privilege. And while that would be true as to the
25 specific information in the draft, they are concerned about

F7M9USAA

1 waiver beyond what was in the draft.

2 THE COURT: All you have to do is just allege whatever
3 information you gave them. You don't necessarily need the
4 draft.

5 MR. GOLDFARB: I'm sorry?

6 THE COURT: All you have to do is allege what
7 information, in your amended complaint or by affidavit, what
8 information, relevant information you provided them. I don't
9 need --

10 MR. GOLDFARB: What we've alleged was, I believe in
11 Mr. MacCoby's affidavit, is that the draft amended complaint is
12 essentially the same -- the information that's in the amended
13 complaint, the first amended complaint. So the court can look
14 at the first amended complaint, and I've cited you to the
15 paragraphs.

16 THE COURT: Are you saying it's more information than
17 what's in the third amended complaint?

18 MR. GOLDFARB: No.

19 THE COURT: Well then why do I need to look at the
20 first one?

21 MR. GOLDFARB: Your Honor, the question -- the issue
22 of what we disclosed to the government, other than the
23 complaint, is not the issue.

24 The reason that the first amended complaint is
25 relevant, at the time the first amended complaint was filed,

F7M9USAA

1 the original question, before you get to anything else, is were
2 the allegations or transactions in the first amended complaint,
3 had those allegations or transactions been publicly disclosed
4 by one of the specified sources listed in the False Claims Act.
5 At that time --

6 THE COURT: I assume that that's in the third amended
7 complaint.

8 MR. GOLDFARB: I'm sorry?

9 THE COURT: Is there something different about that in
10 the third amended complaint?

11 MR. GOLDFARB: Well there's more detail in the third
12 amended complaint.

13 THE COURT: So what's in the first amended complaint
14 that is not in the third amended complaint? Is there something
15 in the --

16 MR. GOLDFARB: No. There's nothing in the first
17 amended --

18 THE COURT: That's what I'm trying to understand. I
19 mean I got the third amended complaint. You tell me that's the
20 complete -- it has everything in it all the other complaints
21 had.

22 I'm not sure why you say that somehow disclosing the
23 first amended complaint is going to advance this argument one
24 way or the other, other than you just simply telling me what I
25 have in the third amended complaint, that's the same

F7M9USAA

1 information I gave to the government. This part I gave to
2 them, this part --

3 MR. GOLDFARB: The reason I'm telling you that, your
4 Honor, is that they're relying on, as the public disclosure,
5 they're relying on something that was disclosed in 2014.

6 THE COURT: Right.

7 MR. GOLDFARB: The first amended complaint was filed
8 in 2011 before those disclosures. So jurisdiction over the
9 claim was established when the complaint was filed in 2011
10 unless the press release that they rely on was a public
11 disclosure, which it wasn't.

12 Once you rule out the press releases and those things
13 that they originally relied on in their original motion,
14 jurisdiction attached when we filed the first amended
15 complaint. That's the point at which jurisdiction attached
16 over this claim.

17 The fact that there was a disclosure later on, three
18 years later, doesn't divest the court of jurisdiction. And you
19 have to -- and the reason for that is the changes and additions
20 that were made since the first amended complaint. They don't
21 add a new claim. They just elaborate on the preexisting claim.
22 They don't add a new legal theory to the claim. They do not
23 add new elements to the claim. It provides more factual
24 detail; most of which, the overwhelming portion of which, did
25 not come from the DFS consent order or the Manhattan D.A.'s

F7M9USAA

1 deferred prosecution order.

2 THE COURT: I know. But that doesn't seem to be the
3 determinative issue for me. I think we can all agree on this.
4 If we can't, then tell me. That what they disclosed
5 subsequently doesn't help them, and what you found out
6 subsequently doesn't help you. Because that's not the state of
7 affairs when the disclosures were made to the government. So
8 they can't rely on: We made a public disclosure sometime after
9 that. And you can't rely on: My client read three years later
10 in a report that somebody said X.

11 MR. GOLDFARB: Well that's right.

12 THE COURT: So, I don't --

13 MR. GOLDFARB: We also allege in the complaint and say
14 in the affidavits that Mr. Grabcheski's allegations were the
15 source of what led DFS and Manhattan -- the Manhattan D.A. to
16 do that investigation. And that's in the third amended
17 complaint.

18 THE COURT: But that's not determinative either, is
19 it?

20 MR. GOLDFARB: No. That's not determinative. But it
21 certainly rebuts the suggestion that Mr. Grabcheski is riding
22 piggyback and riding the coattails of DFS. They are riding his
23 coattails.

24 THE COURT: This is what I think, and take me into
25 another direction if you think I'm going in the wrong

F7M9USAA

1 direction. But this is where I need guidance for me to sustain
2 this complaint. All I need from you is to tell me where I'm
3 supposed to look so that I can articulate what information that
4 he had at the time, what he found out, and what information
5 that he disclosed to the government. If I can identify that
6 and articulate that in some specificity, with some
7 particularity, then it's sufficient. If I can't, if I just
8 have conclusionary language about I went to meetings and
9 sometimes people raised these issues, that's not going to make
10 it. So, therefore, I concluded that they must have been hiding
11 something. No. It's got to be some evidence of a violation
12 here of a fraud, of a misstatement, of a material misstatement.
13 And in what way did he find out that or did he know and
14 disclose to the government that when they said that they were
15 in compliance with state law, that he knew that they knew that
16 that was false, that was a material misrepresentation being
17 made to the government because of these other facts that
18 existed that he knew at the time and that he disclosed to the
19 government.

20 MR. GOLDFARB: Your Honor, in paragraph 150 to 155 of
21 the third amended complaint it deals with the issue of
22 knowledge.

23 THE COURT: 150 to 155.

24 MR. GOLDFARB: Yes. But also 104 to 126 which deal
25 with the concealment issue. That's also very relevant to the

F7M9USAA

1 issue of knowledge. And it names names of high level officers
2 who are officers of both ALICO and AIG, they were dual
3 officers, that they knew that ALICO, that GMD was involved in
4 activity that was --

5 THE COURT: Who knew that?

6 MR. GOLDFARB: Rod Martin is one. Rod Martin was an
7 executive vice-president of AIG.

8 THE COURT: And he knew what? What's the allegation
9 about him?

10 MR. GOLDFARB: Let me turn to that allegation.

11 THE COURT: Just point me to where that paragraph is.

12 MR. GOLDFARB: If you start -- let me walk you through
13 the scenario as described. This is under the heading: The
14 efforts to conceal the U.S. based insurance business conducted
15 by GMD.

16 THE COURT: What page are you on?

17 MR. GOLDFARB: I'm sorry?

18 THE COURT: What page and paragraph?

19 MR. GOLDFARB: It's on page 31 of the third amended
20 complaint starting at the top of the page. Paragraph 104 is
21 really just the introduction paragraph that says they were
22 engaged in a series of actions to conceal.

23 Then 105, up until 2001, the GMD sales force were on
24 the payroll of a variety of AIG domestic operating
25 subsidiaries.

F7M9USAA

1 And then in 2001, they were transferred, for payroll
2 purposes, to AIG, to the parent. It says they were paid under
3 a specific payroll code. And then, over the next few years,
4 AIG's CFO, initially Howard Smith and subsequently David
5 Herzog.

6 THE COURT: Where are you?

7 MR. GOLDFARB: Paragraph 107 now. Questioned the
8 inclusion of the GMD sales staff and payroll code 032 because
9 they basically didn't want this expense under their fiefdom.
10 And it was complained to them, either directly or through a
11 subordinate who relayed information to them, that the employees
12 were GMD New York employees, based in New York, who serviced
13 the multinational segment of AIG's business on behalf of ALICO.
14 They had to be based in New York because that's where the
15 multinational clients were based. And there had to be many of
16 them. And they had to be there to deal with the clients in
17 New York.

18 As I said, they could not be put onto ALICO's payroll
19 because ALICO was not licensed as an insurer in New York and
20 putting them on ALICO's payroll would jeopardize the regulatory
21 exemptions and tax breaks that ALICO enjoyed under Delaware law
22 which were not available to insurers that transacted insurance
23 in the U.S.

24 If you'll indulge for a moment, I can get you the name
25 of the subordinate who relayed the information, who I believe

F7M9USAA

1 Mr. Grabcheski had direct contact with.

2 Michael Tebbs was the subordinate that is referred to
3 in paragraph 107 who Mr. Grabcheski had direct contact with.
4 And Mr. Grabcheski, I believe, also had direct contact with
5 Mr. Smith and Mr. Herzog, who were the CFO at different times.
6 And Mr. Grabcheski is also aware that the facts were explained
7 to Rod Martin who was simultaneously an officer of ALICO and
8 AIG. And I believe it was Mr. Grabcheski, if I'm not mistaken,
9 had direct -- some of those were as a result of personal
10 conversations that Mr. Grabcheski had with Mr. Martin.

11 THE COURT: Why is this, and you just have to explain
12 this to me because technically I don't know, why is this
13 activity -- why do you say this activity is against the law?

14 MR. GOLDFARB: I'm sorry?

15 THE COURT: Why do you say this activity here is
16 against the law?

17 It doesn't talk about being in violation of law. It
18 talks about being able to get tax breaks.

19 MR. GOLDFARB: Because it says they couldn't be put on
20 ALICO's payroll because ALICO was not licensed as an insurer in
21 New York, but GMD were acting on behalf of ALICO, selling
22 insurance on behalf of ALICO. That's who they were -- for
23 whose benefit they were working. And the insurance that was
24 being sold was ALICO insurance. And the activity -- so the
25 activity that these people were doing in New York was the

F7M9USAA

1 insurance activity that required ALICO to be licensed. They
2 were conducting these activities, selling insurance, marketing
3 insurance, soliciting insurance sales and purchases on behalf
4 of ALICO in New York. And that's activity that's required to
5 be licensed under New York law.

6 The reason that they were put into all of these other
7 companies rather than -- they couldn't be put into ALICO is
8 because ALICO wasn't licensed. But the fact is, even though
9 despite these attempts to put them elsewhere, what we're saying
10 is that in substance they were working on behalf of ALICO. And
11 their activity in New York was insurance activity that's
12 attributable to ALICO.

13 They can certainly -- I'm sorry?

14 THE COURT: Is paragraph seven the manner in which the
15 client obtained this information?

16 MR. GOLDFARB: He acquired the information through his
17 discussions with Mr. Herzog, with other -- as I said, Ken
18 Nottingham, who was an officer of ALICO.

19 THE COURT: More than what's in this paragraph?

20 MR. GOLDFARB: Your Honor, we didn't list every piece
21 of the evidence. We didn't list every piece of evidence. And
22 I don't think we have to list every piece of evidence.

23 He was asked to facilitate the process of where to put
24 the GMD employees, you know, other than ALICO. And as a result
25 of being asked to do that he learned the reason that it was

F7M9USAA

1 being done.

2 I don't think we need to in the complaint allege --
3 identify every specific conversation that he had in the course
4 of however many -- however much time this process took. This
5 is something that went on over a period of years.

6 THE COURT: That sounds compelling but that doesn't
7 tell me anything. So I'm just trying to figure out. You say I
8 should look at his affidavits and I should look at the
9 complaint beyond the complaint.

10 I'm just asking you is there something else that I'm
11 going to see in his affidavit that is going to be other
12 instances where this kind of activity or discussion was going
13 on.

14 MR. GOLDFARB: Well, your Honor, the affidavit
15 describes it. It doesn't list specific instances. I don't
16 think we're required to list specific instances.

17 THE COURT: I'm just trying to figure out whether you
18 want me to rely on this as the sole instance or are you saying
19 that there's something else I should look at.

20 MR. GOLDFARB: No, your Honor. I'm going through it
21 one paragraph at a time. Each paragraph only talks about one
22 thing. You really have to read this whole section, which is
23 paragraphs 104 to 126. You have to read the paragraphs about
24 the New York operations, which are paragraphs 67 to 83.
25 There's more discussion of AIG's knowledge in paragraph 150 to

F7M9USAA

1 155. Those are the portions of the complaint that talk about
2 what ALICO did that constituted the illegality. What evidence
3 there was that AIG knew about it. And that's -- and disclosed
4 to the government -- what was disclosed to the government
5 before, previously, was what was in the first amended
6 complaint, which is basically the same underlying core
7 allegation that ALICO and AIG were involved in unlicensed
8 insurance activity, which was later disclosed in 2014. But it
9 was there from the beginning of this claim.

10 THE COURT: So then tell me why you say that was
11 material.

12 MR. GOLDFARB: Why I say that what?

13 THE COURT: Material.

14 MR. GOLDFARB: It's material because it's -- all the
15 details about what was disclosed to the government when is not
16 material for the purpose of whether we've stated a sufficient
17 claim under the False Claims Act. It's only material --

18 THE COURT: Why is that a material misrepresentation?

19 MR. GOLDFARB: It's a misrepresentation because they
20 alleged -- asserted and alleged, they represented and warranted
21 in the debt reduction agreements that they had all necessary
22 licenses.

23 THE COURT: Right. So that's why I asked you: Why is
24 that a material misrepresentation? Why would it have made a
25 difference?

F7M9USAA

1 MR. GOLDFARB: Well it's material. And materiality is
2 something they didn't raise until their reply. So they didn't
3 tell us before we amended that was the problem.

4 THE COURT: That's why I'm asking.

5 MR. GOLDFARB: Materiality is really a dollar issue.
6 They refer to a hundred thousand dollars -- a hundred million,
7 I'm sorry -- a hundred million dollars was referred to in one
8 part of the complaint. But that's not the only effect of the
9 misrepresentation.

10 THE COURT: That's what I'm asking.

11 MR. GOLDFARB: The other issues about the
12 misrepresentation, in addition to revenue, our argument is the
13 valuation of the company was based on revenue projections. And
14 the revenue projections were based on revenue that was illegal
15 and therefore couldn't be continued. So that loss -- that's
16 one way it was overvalued.

17 It was also --

18 THE COURT: I don't understand what the consequences
19 of that overvaluing are. That's what I'm trying to understand.

20 Two questions. Why was that a material
21 misrepresentation? Because are you saying that they would not
22 have bought this -- they would not have bailed them out if they
23 had known that they were doing this unlicensed activity?

24 MR. GOLDFARB: No.

25 THE COURT: And two, what are the damages that you say

F7M9USAA

1 that the U.S. Government suffered?

2 I'm not sure I clearly understand either why this
3 statement that they were in compliance would have materially
4 affected this agreement with the government; and two, what was
5 the damage that the government sustained as a result of this if
6 their position is well, look, they bailed us out, they bought
7 out the company, kept us afloat, then we bought it back from
8 them and that was what was intended. And whether or not -- if
9 they had bought it for one million dollars, then we would have
10 bought it back for a million dollars. If they had bought it
11 back for a hundred million dollars, we would have bought it
12 back for a hundred million dollars.

13 So where do you say is the damage? And where do you
14 say that this would have materially changed the agreement if
15 they had said well, you know what, we can't really say to you
16 that we're totally in compliance because we might be doing --
17 there are some allegations, or we might be doing some insurance
18 stuff here in New York but we're really not licensed to do
19 insurance stuff in New York. If they told them that, you say
20 the deal would have fallen through?

21 MR. GOLDFARB: It would have been a different deal.

22 Your Honor, our theory -- what we allege in the
23 complaint is that the amount of the debt reduction that was
24 given in the debt reduction agreement, that amount of reduction
25 was based on the valuation of ALICO and AIG -- I'm sorry, AIA.

F7M9USAA

1 And we allege that those valuations were based on the
2 assumption that -- for instance, the revenue projections that
3 they based it on were based on the assumption that ALICO and
4 AIA continue to do the business that they've been doing which
5 we say was illegal and, therefore, that projection was invalid.
6 And they also --

7 THE COURT: Invalid in what way?

8 MR. GOLDFARB: Because --

9 THE COURT: They did make that kind of money.

10 MR. GOLDFARB: Because if the assumption is we're
11 going to continue -- that our projection or determination of
12 the value is based on this revenue stream, if the revenue
13 stream is based on illegal activity, that's not a basis you can
14 use to value the company.

15 THE COURT: But it didn't play itself out that way
16 though. It didn't make a difference.

17 MR. GOLDFARB: The question is not how did it play
18 out.

19 THE COURT: The question is how it played out, because
20 you've got to tell me there were damages to the government, and
21 you've got to tell me that it materially would have affected
22 their judgment because they would have anticipated the
23 consequences of this agreement was going to be something
24 different than what they agreed to.

25 MR. GOLDFARB: Your Honor, damages is determined as of

F7M9USAA

1 the time the debt reduction agreement is entered into.

2 THE COURT: So how did the government lose money?

3 MR. GOLDFARB: Because they got -- the value of what
4 they got was worth less than what they paid in debt reduction
5 and what they contracted.

6 THE COURT: What did they pay that they didn't get
7 back?

8 MR. GOLDFARB: Your Honor, that's not -- the issue is
9 not that. The issue is what -- did they get, in that
10 transaction at that time, did they get something that was worth
11 what it was supposed to be worth. That's the damages. At this
12 point we're going beyond the --

13 THE COURT: I don't know what the alternative scenario
14 is that you're trying to give me though. I'm not sure what I
15 see anything different about the world of the financial
16 collapse that would have been different had they been told we
17 can't exactly say that we're in total compliance.

18 MR. GOLDFARB: Your Honor, the alternative scenario is
19 what the deal would have been if the true facts had been
20 disclosed.

21 THE COURT: What do you say that it would have been.

22 MR. GOLDFARB: I'm saying it would be the lesser --
23 the amount of debt reduction would be less. So, therefore,
24 they would have had --

25 THE COURT: What do you mean by debt reduction?

F7M9USAA

1 MR. GOLDFARB: This was an agreement. The government
2 had previously loaned zillions of dollars to AIG. And these
3 two agreements were to reduce the amount of those zillions by
4 25 billion in return for giving the government these equity
5 interests in AIG and ALICO. And they would -- the allegation
6 is that they would have gotten less of a debt -- there would
7 have been less of a debt reduction so that the debt -- the debt
8 that would have had to have been paid back would be more than
9 it would have been if the truth had been disclosed.

10 THE COURT: I just don't know how you came up with the
11 hundred million dollars in relationship to that.

12 MR. GOLDFARB: The hundred million dollars has to do
13 with one figure in terms of amount of profit that was received,
14 generated by GMD with regard to certain business. That's
15 quantifying to some extent -- it's actually not a complete
16 quantification, but quantifying, putting a dollar value on some
17 of the illegal business.

18 But in addition to the revenue, there's also they
19 failed to disclose the liabilities, the potential liabilities
20 that ALICO and AIG faced because they were engaged in this
21 illegal activity.

22 THE COURT: But the government never suffered those
23 liabilities.

24 MR. GOLDFARB: But the government -- it's not the
25 question whether the government suffered those liabilities.

F7M9USAA

1 THE COURT: Well, it. It's a question of damages.
2 That's not part of your damages.

3 MR. GOLDFARB: The damage is -- the measure of damages
4 is determined at the time of the deal. It's not determined
5 based on facts --

6 THE COURT: But it's determined as a loss.

7 MR. GOLDFARB: Right. And the loss that we're saying
8 happened is that what the government got for its reduction was
9 overvalued. If you buy property and it's overvalued, you've
10 been damaged because instead of getting something that's
11 supposed to be worth a million dollars you're getting something
12 that's worth half a million dollars. In that case you're
13 damaged by half a million dollars. And we're talking different
14 numbers, but that's essentially what's happening here.

15 They contracted to pay -- to buy -- it's sort of buy
16 in quotes because they paid for it by debt reduction, but they
17 contracted to buy something worth X and what they got was
18 something that was worth less than X. And that's the classic
19 form of fraud damages.

20 There's Second Circuit case law that says that's
21 the -- the measure of damages in a False Claims Act case. And
22 you don't look at down the line what happened later on. You
23 look at damages as of the time that the transaction is
24 undertaken.

25 THE COURT: But those damages clearly can't be

F7M9USAA

1 measured by the purchase price.

2 MR. GOLDFARB: Well that's one piece of it.

3 THE COURT: Because they got that paid back. That's
4 not the question.

5 The question would be what was the loss amount -- if
6 you say that they owed the government a hundred million dollars
7 and they forgave \$50 million of that. And otherwise if they
8 had known that this company was doing illegal activity, they
9 would not have forgiven \$50 million of that, they would have
10 only forgiven \$25 million of that. I mean I have some doubt
11 that that's really the kind of thing you're going to be able to
12 establish on the basis of what really occurred here ultimately.
13 I can understand that.

14 Obviously, it doesn't have anything to do with them
15 just giving them loans or purchasing an interest in the company
16 because they didn't suffer a loss as a result of that. And
17 they would not have -- it is no reason to conclude that they
18 would have not done this deal had they known that they were
19 involved in illegal insurance business. That's not what you're
20 arguing.

21 MR. GOLDFARB: No. We're not saying the deal would
22 not have been done. It would have been a different deal.

23 THE COURT: The purpose of this deal was not for the
24 U.S. Government to make money.

25 MR. GOLDFARB: No. But they're entitled to get what

F7M9USAA

1 they contract for. The government is entitled to get what it
2 contracts for.

3 THE COURT: Right.

4 MR. GOLDFARB: It's entitled not to be defrauded when
5 it does the deal, no matter what the purpose of the deal, you
6 know, it's entitled to that. The statute, in addition to just
7 the common law of fraud, the False Claims Act entitles them to
8 that. So it makes it illegal to defraud the government.

9 This is an issue that hasn't been briefed because it
10 wasn't raised until AIG's reply, and it really goes beyond
11 what's in the complaint. I would suggest -- maybe we could
12 submit a letter that would lay out the argument because I
13 haven't had a chance to give those cases, and I don't have them
14 with me right now.

15 THE COURT: Well can you can submit -- on the same
16 schedule that they are going to submit their letter on the
17 other issue, you can submit a letter.

18 MR. GOLDFARB: So that deals with the damages theory.

19 To get back to the issue of materiality. That really
20 is a question, as they framed, of whether the dollar amounts
21 are, you know, of the overvaluation are enough that it would
22 have made a difference. And we have alleged -- in addition to
23 that hundred million dollar figure there is tax liability that
24 we have alleged; that they weren't paying taxes on U.S. income
25 that would have been taxable by the feds and by states. And

F7M9USAA

1 that there was potential liability to state governments such as
2 occurred with the consent orders and deferred prosecution
3 agreements, which we realize were settled, but that
4 certainly --

5 THE COURT: But those were not settlements with the
6 federal government.

7 MR. GOLDFARB: No. But that shows, that's the kind of
8 liability that would have contributed -- the likelihood of that
9 liability affects the valuation of the company. Because one of
10 the things that was --

11 THE COURT: But the U.S. Government didn't pay that
12 liability.

13 MR. GOLDFARB: No. But it entered the debt reduction
14 agreement based on a warranty that the liabilities had been
15 disclosed in the financial statements, which we don't think
16 happened because they didn't disclose we're facing zillions of
17 dollars of liability to the federal government in taxes, to the
18 New York government in fines.

19 Also, one of the representations and warranties was
20 that they had adequate reserves.

21 THE COURT: Well, you don't allege that that's part of
22 the false claims.

23 MR. GOLDFARB: Well, it's part of what makes it false
24 because we say, because they were -- because of the fact they
25 weren't licensed they weren't following the reserve

F7M9USAA

1 requirements.

2 For instance, give an example. In Delaware they were
3 exempt from the ordinary reserve requirements for insurance
4 companies because the position they took with the Delaware
5 government was we're only doing insurance business overseas so
6 there's a statutory exemption in Delaware that as long as
7 you're not doing insurance business in the U.S. you only have
8 to comply with the reserve requirements in all those different
9 countries where you're doing business.

10 THE COURT: But that wasn't part of your client's
11 disclosure.

12 MR. GOLDFARB: It was not in the first amended --

13 THE COURT: Well, it wasn't part of your client's
14 disclosure at all. He was not the original source for that
15 information. And he didn't disclose that information to the
16 government. He wasn't the source, original or otherwise, of
17 that information.

18 MR. GOLDFARB: He doesn't have to be. If the original
19 source issue comes up, he doesn't have to be the original
20 source of everything. He has to be the original source of the
21 core allegations, as the Second Circuit said.

22 THE COURT: He said that they were not in compliance
23 in New York and he had information.

24 MR. GOLDFARB: And also said they weren't in
25 compliance in Delaware.

F7M9USAA

1 THE COURT: He did also tell the government that --

2 MR. GOLDFARB: Yes.

3 THE COURT: Based on what?

4 MR. GOLDFARB: Based on that they were doing
5 underwriting activities in Delaware.

6 THE COURT: I didn't see that. Where is that?

7 MR. GOLDFARB: That's in the first amended.

8 THE COURT: Well is it in the third amended?

9 MR. GOLDFARB: It's in both, your Honor.

10 THE COURT: Where is it in the complaint that it says
11 that he -- that they weren't in compliance in Delaware?

12 I don't think it says that he disclosed that. And I
13 don't even think -- does his affidavit even say that?

14 MR. GOLDFARB: Well, no. The affidavit talks about
15 how it was that he knew the information.

16 THE COURT: Yeah, but it doesn't talk about the
17 Delaware information. He doesn't say he knew the Delaware
18 information.

19 MR. GOLDFARB: Right. Because the Delaware -- it's
20 not relevant whether -- in order for the question to come up
21 whether he's the original source of the Delaware information,
22 first there has to be a public disclosure of the allegation or
23 transaction. And the only thing they've pointed to as that, as
24 a public disclosure, is a statement in the examination report
25 by Delaware which doesn't say that they were doing underwriting

F7M9USAA

1 activity --

2 THE COURT: I know, but that's not -- I don't even
3 know why we even have to debate about Delaware because it's not
4 your contention that your client found out about Delaware and
5 disclosed Delaware to the government; is it?

6 MR. GOLDFARB: It's in the first amended complaint.

7 THE COURT: That he knew about activity going on in
8 Delaware?

9 MR. GOLDFARB: Yes. That was -- it's in the first --

10 THE COURT: Where is that?

11 MR. GOLDFARB: Your Honor, if you'll indulge me --
12 maybe if I could submit the paragraph rather than take the time
13 to look now.

14 THE COURT: Are you saying that's in the complaint or
15 in his affidavit?

16 MR. GOLDFARB: I believe it's in the first amended
17 complaint and the second and third amended complaint.

18 THE COURT: That he knew about Delaware activity and
19 he disclosed that to the government?

20 MR. GOLDFARB: Well, yes, because the disclosure to
21 the government is the, among other things, a disclosure of the
22 draft first amended complaint which was disclosed before the
23 draft --

24 THE COURT: What do you mean the disclosure of the
25 draft?

F7M9USAA

1 MR. GOLDFARB: Well we provided a copy of it to the
2 government before we filed it. That's a disclosure to the
3 government.

4 THE COURT: But, again, you're confusing me because
5 you keep saying there's nothing in that complaint that's not in
6 this complaint.

7 MR. GOLDFARB: That's right. But there's also --

8 THE COURT: So why am I --

9 MR. GOLDFARB: There's a lot in the third amended
10 complaint. There is stuff in the third that's not in the
11 first.

12 THE COURT: I understand that. But I didn't see a
13 reference to Delaware. Maybe I didn't look at it as closely.

14 MR. GOLDFARB: Would the court indulge -- if the Court
15 will indulge me I'll find the paragraph number.

16 THE COURT: I think I did find it. I'm sorry. I
17 apologize. I think it's on page 13.

18 MR. GOLDFARB: Which document are you looking at?

19 THE COURT: I'm looking at the third amended
20 complaint.

21 MR. GOLDFARB: What paragraph?

22 THE COURT: Paragraph 46.

23 MR. GOLDFARB: That lays out what Delaware law is.

24 THE COURT: That's reference to Delaware. That's all
25 right. I can look at that.

F7M9USAA

1 MR. GOLDFARB: I'll be glad to submit if the Court
2 would like a letter.

3 THE COURT: That's not determinative either way.
4 You're arguing now about Delaware. I mean he didn't make
5 disclosures about other states. The one paragraph you pointed
6 to me was that he was told why they were trying to cover up
7 New York business because -- for the reasons that you gave.
8 But you don't say that there are similar conversations about
9 activities in other states that he was aware of.

10 MR. GOLDFARB: Your Honor, you're right.

11 Let me explain the reason why Mr. Grabcheski's
12 declaration talks about what it does and why it doesn't talk
13 about other things. And that's because if there's -- unless
14 there's a prima facie showing of a public disclosure, original
15 source is irrelevant. We don't have to do anything.

16 What they produced about Delaware, the only thing they
17 pointed to is that excerpt from the examination report which is
18 not a prima facie disclosure. So we determined we don't need
19 to disclose -- say anything about Delaware. If the Court finds
20 that that was a public disclosure by Delaware, then we're in a
21 different situation. But we think it's clear that it was not.

22 THE COURT: They have to give me a relevant public
23 disclosure before he makes his disclosure to the federal
24 government.

25 MR. GOLDFARB: Before it triggers the original source.

F7M9USAA

1 And that's the point at which it makes a difference about what
2 was told to the federal government.

3 Unless the court has any more questions about that
4 aspect, let me talk about some additional issues.

5 One of the points they've made is -- before I get to
6 that. Just to lay out, just so the Court understands our
7 position about --

8 THE COURT: Let me just find out. How much more time
9 are you going to want to need, because either we're going to
10 adjourn for lunch and come back or we can wind up in the next.

11 MR. GOLDFARB: Fifteen minutes.

12 Maybe it would be better if we did it after lunch so I
13 don't have to keep leaning over to hear my client.

14 THE COURT: Why don't we do this. Let's adjourn for
15 an hour. 2:15. So I will give you a full opportunity to be
16 heard.

17 (Luncheon recess)

F7M9USAA

1 AFTERNOON SESSION

2 2:25 p.m.

3 THE COURT: Yes, sir.

4 MR. GOLDFARB: Thank you, your Honor. Your Honor
5 Mr. MacCoby has some kind of emergency. I'm not sure if he'll
6 be back or what the story is.

7 Just to pick up where we left off, on the issue of the
8 Delaware allegations. That's paragraphs 81 through -- I'm
9 sorry 88 through 91 of the third amended complaint.

10 Now, your Honor, I think -- as we said, I think that
11 the detail the court has been asking for is not required in the
12 complaint. And frankly, if the Court's asking did we allege,
13 you know, Mr. Grabcheski found XYZ facts from one person and he
14 found ABC facts from another person, that level of specificity,
15 that's not in the complaint, and it's not in the declaration.
16 We don't think it has to be. But we absolutely can provide
17 that if the Court allows another amendment. And I think that
18 makes sense because I think that the Court would clearly -- I
19 can see now what the court has focused on -- I don't know if
20 they were the only issues, but certainly some very major
21 issues. And I think I can represent I think we can provide
22 that information. Certainly Mr. Grabcheski can -- you know,
23 has the information about who told him what. And if the Court
24 would like, I can proffer some of it now to give an example.

25 But I think it would be best to, if we have that

F7M9USAA

1 opportunity, that we could give a complaint that really does
2 lay out what we think -- what he found out, how he found it
3 out, and what was disclosed to the government at what point.

4 THE COURT: I'm just trying to figure out in what
5 manner you have alleged fraud with particularity.

6 MR. GOLDFARB: That's right. I understand that.

7 THE COURT: It can't simply be I think they violated
8 the law or I accuse them of violating the law or I accuse them
9 of saying that -- I accuse them of falsely saying that they
10 have complied with the law and they didn't comply with the law.
11 It's got to be -- a pleading with particularity is who did
12 what, who said what, what were the misrepresentations, who
13 relied upon them.

14 MR. GOLDFARB: Your Honor, in terms of the
15 particularity, I mean the who, what, where, that relates
16 primarily to the fraudulent statements. And that we've alleged
17 very particularly. We've identified two specific documents,
18 the debt reduction agreements. We have the date they were
19 executed. We've made allegations about the place they were
20 executed. We've alleged who signed it. It's visible on the
21 complaint.

22 Most frauds -- a lot of frauds, certainly, the
23 statements are made orally. There is general -- you know,
24 there's an issue of particularity. But we've got the specific
25 documents. There is no doubt about -- no possible dispute or

F7M9USAA

1 uncertainty about where and when and how the fraudulent
2 statements were made and what they said.

3 THE COURT: Well I think one of the issues that I have
4 is it's unclear to me who is supposed to have some scienter
5 here.

6 MR. GOLDFARB: I can address that.

7 THE COURT: You can't just simply say AIG defrauded
8 the government. You've got to give me with some particularity
9 the scienter over whose part that you say connects the dots in
10 terms of knowing the truth, making the false statements,
11 knowing the false statements were intended to mislead.

12 It can't be that person A made a statement and that
13 wasn't true, person B knew it was false, and person C was the
14 person who was hiding it. You've got to connect it all.

15 MR. GOLDFARB: Yes, your Honor.

16 THE COURT: I'm not quite sure who you're accusing of
17 knowingly making the false statement to the government.

18 MR. GOLDFARB: Let me address that, your Honor.

19 First of all, just on a broad level of the law, to
20 what extent are we allowed to aggregate different people's
21 knowledge. That's the collective knowledge issue. The case
22 that AIG relies on, what the rule is you cannot aggregate --
23 you can't take everybody in the company and say whatever
24 anybody knows, we can put that together, even if it's totally
25 innocent knowledge. That's clearly not allowed. That's not

F7M9USAA

1 what we've done.

2 We've identified very specific, high level officers,
3 such as Rod Martin, who is an executive vice-president of AIG
4 and was also a high level officer of ALICO; David Herzog, who
5 is the chief financial officer of AIG; Chris Swift who was a
6 vice-president of AIG. All of those people we allege had
7 knowledge of the illegality. And we describe some of the
8 circumstances in the discussion of concealment, which -- how
9 they got that knowledge.

10 THE COURT: But you have to connect those people not
11 just with the illegality. But you have to connect them to the
12 false statements.

13 MR. GOLDFARB: That's right.

14 We do that, your Honor. We allege that they were
15 aware of the debt reduction agreement and of the written -- the
16 representations that were made. And that's enough. In the
17 Harrison, U.S. ex rel. Harrison, which is cited in the case
18 that AIG has cited, the Science Applications case, said you
19 don't have to show that the person who actually signed the
20 claim had the knowledge.

21 So the fact that the chief financial officer, for
22 instance, who had knowledge of the underlying facts also was
23 aware of the debt reduction agreement. That's what chief
24 financial officers --

25 THE COURT: But that's not sufficient. They have to

F7M9USAA

1 be more than aware of the debt reduction agreement. They have
2 to be aware of the representation that's made in the debt
3 reduction agreement. You can't just simply say they know
4 there's an agreement. They have to be aware that a statement
5 was made in the agreement that they knew was false.

6 MR. GOLDFARB: Well the complaint alleges that.

7 But there's also the fact that knowledge is defined in
8 the False Claims Act not only as actual knowledge but also
9 reckless disregard of the truth and willful blindness as to the
10 truth.

11 THE COURT: I'm not sure I can read from your
12 complaint that you're alleging any factual circumstance other
13 than actual knowledge.

14 MR. GOLDFARB: Well, I mean we specifically say --

15 THE COURT: You weren't willfully blind. There is no
16 fact that you put in here that would make them willfully blind
17 as opposed to knowingly making a falsehood. Either they knew
18 that they were complying with the law or they didn't know they
19 were complying with the law the way you've alleged it. They
20 didn't stick their head in the sand and not care. You
21 specifically allege that they deliberately made this falsehood
22 knowing the facts were different.

23 MR. GOLDFARB: Your Honor, the complaint -- we
24 actually say that, as used in the complaint, we're using
25 knowledge to include either actual knowledge or reckless

F7M9USAA

1 disregard or willful blindness.

2 THE COURT: Give me a plausible scenario that this
3 would be willful blindness under the facts that you've given
4 me.

5 MR. GOLDFARB: Let me give you -- one plausible
6 scenario has to do with the person who signed the debt
7 reduction agreements on behalf of AIG was, I think it's Paula
8 Reynolds, who was the chief restructuring officer. And she
9 certainly had, before signing that agreement, had a duty to do
10 due diligence.

11 THE COURT: But that's not willful blindness.

12 MR. GOLDFARB: Let me finish out the scenario.

13 So that would require finding out, asking people what
14 the answer -- are these representations correct. And
15 certainly -- and it's also, the chief financial officer, it's
16 within the scope of his duties to sign off on a major deal like
17 this. He needs to know what it contains.

18 These kind of representations are not unusual
19 representations. The representation that insurance companies
20 got licenses, they're operating lawfully, they are absolutely
21 standard representations in major deals like that. So they've
22 got to know that these representations are being made.

23 THE COURT: What's the factual scenario that you
24 allege -- wait.

25 What's the factual scenario that you allege is willful

F7M9USAA

1 blindness?

2 If I know that they're making a representation in the
3 agreement that they're in compliance with state law, based on
4 the way you've alleged this complaint, in what way can I not --
5 can I be liable and not know that the statement is not true?

6 MR. GOLDFARB: I'll tell you -- first of all, your
7 Honor, knowledge does not have to be alleged with
8 particularity. It can be alleged generally.

9 One scenario -- you've asked for a scenario. I'll
10 admit this is not spelled out in the complaint.

11 THE COURT: That's what I meant, a scenario that
12 you've laid out on the facts that you've alleged -- I cannot
13 read this complaint and come away from it with: Oh, this is
14 willful blindness. I read this complaint and come away from it
15 that they knew and they deliberately made a false statement
16 that they knew is not true because they were intentionally
17 covering it up. That's the only scenario.

18 MR. GOLDFARB: An inference that you can draw from
19 the -- one inference, I'm not saying it's the only inference --
20 is that Paula Reynolds, either she didn't ask are we in
21 compliance, and that's either recklessness or willful -- you
22 know, deliberate blindness.

23 THE COURT: Why would I read that from your complaint.
24 Your complaint doesn't say that. It doesn't even imply that.
25 It doesn't imply that she didn't ask.

F7M9USAA

1 MR. GOLDFARB: Your Honor, I'm saying the possible
2 scenarios; that you can infer that either she did ask or she
3 didn't ask. If she did not ask, that's either willful
4 blindness or reckless disregard.

5 THE COURT: I can't infer that because you don't
6 allege it.

7 MR. GOLDFARB: If she did ask and she was told the
8 truth, then she knew about it and --

9 THE COURT: That seems to be the only --

10 MR. GOLDFARB: If she did ask and was not told the
11 truth, then AIG is tagged with that dishonesty of the person
12 who didn't tell her the truth.

13 THE COURT: But that's not what you allege. Right. I
14 mean that's not what you accused them of doing.

15 MR. GOLDFARB: Your Honor, it's not spelled out.

16 THE COURT: That's not what you intended -- that's not
17 even what you intended to imply.

18 You specifically said they knew that they were in
19 violation of the law. And they made a deliberate decision to
20 say that they weren't, they were in compliance with the law.
21 That's what you've alleged. That's the only thing you've
22 alleged.

23 MR. GOLDFARB: Perhaps -- I thought -- we tried to
24 make it clear and perhaps it was not as clear as it should have
25 been.

F7M9USAA

1 We did specifically say that knowingly -- we said this
2 in the complaint.

3 THE COURT: Did you say that somebody at AIG was
4 willfully blind to this?

5 MR. GOLDFARB: We said that, as used in the complaint,
6 knowingly or knowledge includes reckless disregard and willful
7 blindness.

8 THE COURT: I'm not talking about a definition. I'm
9 talking about a factual allegation.

10 MR. GOLDFARB: I didn't spell out those scenarios
11 explicitly but we've got -- again, I think given that knowledge
12 can be alleged with generality, I think that what we've said is
13 sufficient. I don't think we need to spell it out at that
14 level of detail.

15 And we do specifically allege that Mr. Herzog,
16 Mr. Martin, and Mr. Swift, who were very high officers at AIG,
17 were aware not only of the illegality but aware of the debt
18 reduction agreement and aware of the representations.

19 THE COURT: I don't know what the basis of that
20 allegation is.

21 That's an assumption. But I don't know where that
22 factual allegation comes from. You're assuming that. You
23 don't have any proof of that.

24 MR. GOLDFARB: Your Honor, perhaps we should have put
25 information and belief.

F7M9USAA

1 THE COURT: But even with information and belief,
2 you've got to tell me on what kind of information that you.

3 MR. GOLDFARB: Certainly with regard to -- there's
4 several things.

5 First of all, Mr. Herzog as chief financial officer
6 making this kind of a decision whether to sell a subsidiary --
7 because this is all in the context of selling -- planning to
8 sell ALICO and AIA.

9 THE COURT: But you have to acknowledge that that
10 would be an insufficient basis to make a sufficient allegation.
11 If that was true -- and quite frankly I hear that argument
12 plenty of times. If that were true, every single person who
13 was a high level officer, there would be some inference that
14 they would be involved in fraud because they are a high level
15 official and should have known.

16 That's not the test here. You can't do it that way.
17 There's got to be some reasonable inference based on some facts
18 that would give that particular person personal knowledge or
19 some willful disregard of the truth or something.

20 I can't say that somebody stealing money out of
21 Microsoft, that the natural inference is that Bill Gates knows.
22 That's not the way it works. You know that that's not the way
23 it works.

24 I have to go behind the reference to AIG and analyze
25 the individuals that you say are the actors on behalf of AIG to

F7M9USAA

1 look at the conduct and their knowledge and their scienter.
2 Because companies are fictions. They are not people. They
3 don't act. They don't talk. They don't speak. They don't
4 take actions. They do it through individuals.

5 I'm trying to give myself a mental chart of who are
6 the links, individuals in this chain that you say makes AIG
7 responsible for knowingly or recklessly making false
8 representations in the document that's only signed by a limited
9 number of people.

10 Who are the conspirators here?

11 MR. GOLDFARB: Your Honor, I think certainly the chief
12 financial officer is -- straight in the core scope of his
13 duties to be involved in a major, enormous transaction,
14 billions and billions of dollars, the chief financial officer
15 is going to be involved in that. And that's not just
16 speculation. That's what CFOs do.

17 THE COURT: That's not an inference of scienter. You
18 can't make that an inference of scienter. Of course they are
19 going to be involved with it. Every time something goes wrong,
20 just because the person is the chief financial officer you
21 can't say: Well, they're the chief financial officer, they
22 should have known. "Should have known" is not the test.

23 MR. GOLDFARB: Mr. Grabcheski told Mr. Herzog himself
24 about the illegality of the conduct. So in that case we --

25 THE COURT: Again that's why I ask these questions.

F7M9USAA

1 Is that either in the complaint or in his affidavit, or is that
2 something you're informing me of now?

3 MR. GOLDFARB: Your Honor, that level of detail I
4 don't think is in the complaint.

5 THE COURT: Well any level of detail. There is no
6 place that he says that I read that he was told by this person.
7 You're informing me of that now.

8 I mean I accept your representation of that. I just
9 didn't -- that's news to me.

10 It could be there. If it is, I'd like to look at it
11 specifically.

12 That's fine. I agree with you. Obviously, knowledge
13 by a high level AIG official that the operations were not in
14 compliance with the law and a statement saying -- in the
15 agreement saying that they were in compliance with the law may
16 be enough. I'm not going to say it's necessarily enough
17 because it depends on how you link the two and whether or not
18 you have the combination of people that will make AIG as an
19 entity liable for the misstatement. But I'm not going to say
20 that necessarily the person who makes the misstatement has to
21 be the same person he spoke to for that to sustain, at least
22 initially, the complaint. But I've got to have, as I say, link
23 in this chain of having someone demonstrating that they had the
24 knowledge, and that person having such a capacity that it would
25 be unlikely that someone else on behalf of the company would

F7M9USAA

1 make this representation without knowing the information that
2 that person knows and should be attributed to that person.

3 MR. GOLDFARB: Your Honor, as far as what's in the
4 complaint -- the third amended complaint that goes -- there's
5 two places where we talk about the knowledge. One is
6 paragraphs 104 through -- that section about the concealment,
7 104 through 122, I think. And then the other one is paragraphs
8 150 through 155.

9 155 talks generally in terms of this was a topic of
10 discussion, there were meetings. It doesn't get more specific
11 than that.

12 The earlier set of paragraphs, 104, in that section,
13 that does talk about more specifically about circumstances in
14 which David Herzog for instance and Chris Swift and Rod Martin
15 found out. It doesn't say, I don't think, that Mr. Grabcheski
16 told them anything. It says they knew.

17 We can provide -- we think what we've given is enough
18 but we could certainly I think provide the level of detail that
19 your Honor is asking about.

20 THE COURT: What paragraphs?

21 MR. GOLDFARB: 104, that section, section D that
22 starts at 104.

23 THE COURT: Right. We looked at that.

24 MR. GOLDFARB: So 104 to 112. Two pages. I'd
25 particularly call your attention to those two pages.

F7M9USAA

1 THE COURT: The real question for me, part of the
2 important question is I have to be confident that this is
3 something that your client knew rather than surmised.

4 MR. GOLDFARB: Yes. I understand.

5 THE COURT: That's the thing. I need that level of
6 detail. It can't be just I figured it out. It's got to be
7 that I had specific knowledge and specific facts that if I gave
8 those facts to the government the government would have a basis
9 to bring this complaint.

10 MR. GOLDFARB: Yes.

11 THE COURT: That's the way I'm trying to handle it.

12 MR. GOLDFARB: To the extent that we have not done
13 that, if the complaint doesn't do that, I can proffer that I
14 think we can do that if the court gives us another opportunity
15 to amend.

16 Mr. Grabcheski was certainly present there, and
17 operating at a high level, and interacting with high level
18 management people and did, in fact, have the kind of
19 conversations that the court is talking about.

20 And I think a better way to present that than me
21 making proffers in court would be to allow us another chance to
22 amend. And it will be in the complaint in black and white and
23 it's not -- at that point we certainly understand the court's
24 concerns and have a very specific target to be aiming for. So,
25 as I said, I do think that would be the best thing to do. And

F7M9USAA

1 then certainly the court -- I think that -- if we can't do it
2 then, we're not going to be able to do it. There will be no
3 doubt at that point. If the court thinks that's not enough,
4 then I think at that point there's not going to be anything
5 more we can do.

6 THE COURT: I agree with you that everything that
7 establishes his status to bring this lawsuit doesn't have to be
8 in the complaint. I agree with you with that. I didn't mean
9 to give you that impression.

10 Even if I analyze this complaint as if it was the
11 government bringing this complaint, I still would demand of
12 them some specific factual allegations that would lead to the
13 probable conclusion that these people knew, made the false
14 statement, this is how they knew, this is the particular false
15 statement they made.

16 Because this is -- this is the more general rather
17 than the more specific false statement kind of allegation.
18 This isn't like: Well our company has ten trucks in their
19 warehouse and we only have one truck in the warehouse, we have
20 no trucks in the warehouse. This is: Oh, we complied with
21 state law.

22 That's sort of general statement about being in
23 compliance with state law demands a little more specific -- not
24 a little more than what you have, at least more specific than
25 the example I gave you of, okay, what is the nature of the

F7M9USAA

1 information and the noncompliance that really puts the lie to
2 that statement. If it said -- if the agreement said we're in
3 compliance with all state laws and I know that our truck driver
4 ran a red light yesterday, no you don't have a material false
5 statement or a fraud. So the question really also is whether
6 or not the nature of what you say is the unlicensed -- you
7 allege is the unlicensed insurance business is such that it is
8 the kind of thing that is specifically deemed represented to be
9 in compliance rather than -- that saying that we are in
10 compliance with the law is a representation that we are doing a
11 licensed insurance business rather than we are doing an
12 unlicensed insurance business.

13 MR. GOLDFARB: That's right. But there was -- we did
14 allege, and there is a representation and a warranty in the
15 agreements that they had all necessary licenses. So it wasn't
16 just we complied with the law. The agreements did focus in on
17 the licenses.

18 As I said, I think we can provide the kind of detail
19 that you're asking about. So we'd ask for that opportunity to
20 do that.

21 If I could, I'd like to move on to one of the -- a
22 couple of the additional other issues that Mr. Burck raised.
23 One has to do with his argument that the New York statute
24 wasn't clear and they had a reasonable interpretation that if
25 they were doing this activity they didn't have to be licensed.

F7M9USAA

1 And his argument, as I understand it, is that the statute
2 doesn't clearly say that if the insureds and the risks are
3 located outside of New York that you still have to be licensed
4 if you're doing the sales and marketing in New York. That's
5 simply wrong.

6 The statute -- first of all, in defining what's an
7 insurance business in New York, and this is New York Insurance
8 Law Section 1101(b)(1), it says doing any of the following
9 acts, and it includes making or proposing to make as insurer
10 any insurance contract, including issuance or delivery of a
11 policy or contract to a resident of the state, and that's what
12 Mr. Burck relies on. But then it goes on to say, "or to any
13 firm, association, or corporation authorized to do business
14 herein."

15 So that, by definition, includes foreign companies.
16 It doesn't say any companies incorporated in New York. It says
17 authorized to do business in New York. So a Delaware
18 corporation, dozens, hundreds of them are authorized to do
19 business in New York.

20 THE COURT: I'm not sure that that's a determinative
21 factor for me because I'm not sure -- I'm not convinced that I
22 can resolve their good faith or reasonableness on the face of
23 this complaint on this motion. If that's their defense, that's
24 their defense.

25 Your complaint doesn't allege that they're acting

F7M9USAA

1 reasonably. Your complaint alleges that they're acting
2 deliberately in violation of the law and making false
3 representations.

4 MR. GOLDFARB: There is also -- there were
5 department -- the regulators gave publicly available advisory
6 opinions that were very clear that said this did cover activity
7 even where the insured is located out of the country.

8 THE COURT: How do I resolve that?

9 MR. GOLDFARB: There is also this -- this I think
10 makes it unmistakably clear. If I could hand up -- this is
11 just an excerpt from the statute. I've given a copy to
12 Mr. Burck. The first paragraph is just the section I read
13 before. Section 1101(b)(2) is two of the exceptions to the
14 definition. And you'll see that those exceptions talk about
15 situations under certain circumstances where the risk or the
16 insured is located out of the state, that in those cases under
17 certain conditions you don't need a license.

18 Well, obviously if out-of-state risks aren't within
19 the definition to begin with, you don't need an exception for
20 them. The fact that they put in an exception covering those
21 kind of risks in certain conditions, which don't apply here,
22 but the fact that they put those exceptions in, that
23 conclusively shows that the statute covers a situation where
24 there's activity in New York that is insurance business and the
25 risks and the insureds are located out of New York.

F7M9USAA

1 So given that, together with the first section,
2 together with the advisory opinions, there is no reasonable,
3 possible reasonable argument that they could have believed that
4 it wasn't necessary to get a license. So I just think that
5 point needs to be made.

6 Even if they did -- that still gets to the question
7 even if there might have been a reasonable argument, what did
8 they think the law was. And that is a factual question. And
9 we do allege that they -- that their understanding of the law
10 was that a license was required.

11 In terms of the falsity of the representations,
12 assuming the court -- the question then is, is the activity
13 that we've alleged, does that constitute activity that would
14 require licensing.

15 We alleged it was marketing activity, it was
16 solicitation. We said it was on behalf of multinational
17 corporations. We named about a half a dozen corporations that
18 were clients. We said they made phonecalls, they made sales
19 calls, they went out and visited the clients in New York,
20 negotiated the terms of an agreement. So we've given more than
21 just a general description of the kind of activities that went
22 on. We've been very specific.

23 So when you compare that, especially to the advisory
24 opinions and the kind of activities that are described there, I
25 think it's very clear that what they were doing did require a

F7M9USAA

1 license.

2 Now with regard to the issue of materiality. Based on
3 a conversation I had with Mr. Burck I don't know if I misspoke
4 or it wasn't totally clear but I want to make sure to clarify
5 something I said about the fact of when they raised the
6 argument about materiality. They raised it in the most recent
7 filing which was their opposition to our motion for leave to
8 amend and combined with their reply in support of their motion
9 to dismiss.

10 I don't mean to contend that they hadn't raised the
11 issue before today. They did raise it then. But that was
12 after -- that was not included in their initial motion to
13 dismiss. So when we drafted the third amended complaint we
14 didn't -- you know, we had no notice that they were contending
15 our materiality allegations were deficient.

16 THE COURT: I thought you replied to that.

17 MR. GOLDFARB: Well, we replied -- we replied -- yes,
18 we did reply, make a legal argument. What we did not do was to
19 file yet another request to amend at that point. We had
20 already submitted our third amended complaint which did not
21 make any changes regarding materiality because at that time
22 they hadn't raised the issue. So, my point was just we hadn't
23 really had a fair opportunity to meet the objection. If the
24 court found the objection was well taken, we didn't have an
25 opportunity to make another amendment. So that would be

F7M9USAA

1 another, I guess, point in support of a request for leave to
2 amend that, if we're granted it, we would be able to address
3 that issue and those are the kind of questions that the Court
4 raised before lunch.

5 If I can have the Court's indulgence for a minute.

6 (Pause)

7 That's all I have, your Honor.

8 THE COURT: Thank you. Mr. Burck do you want to
9 reply.

10 MR. BURCK: I will try to be very brief, your Honor.

11 Just a few points. I'll take it backwards because it
12 was a long argument.

13 The last point about materiality. We didn't raise
14 materiality in our motion to dismiss because they didn't
15 specify any statute that we violated. So when we did our
16 motion to dismiss, they then responded and said okay well
17 forget the second amended complaint, we'll do the third amended
18 complaint. That's when they added the provisions from the
19 consent orders. So then we raised materiality. They did, as
20 the court said, have an opportunity to respond in the brief.
21 That's just a small point, your Honor. I'll do another small
22 point before I get to the broader point.

23 On the New York insurance law argument -- this is one
24 of the reasons why I believe the Court is absolutely correct,
25 that this is not the place to be assessing the legal arguments

F7M9USAA

1 on New York state law.

2 Mr. Goldfarb said that -- he pointed to this provision
3 in 1101 where he said that the reason why we should have known
4 that we couldn't market to companies located in New York was
5 because -- he read from this part of the statute. We were
6 making or proposing to make as insurer any insurance contract,
7 including either issuance or delivery of a policy or contract
8 of insurance, to a resident of this state or -- this is the
9 provision he thinks is important -- or to any firm,
10 association, or corporation authorized to do business herein.

11 The problem, your Honor -- the reason we're raising
12 this is to highlight the point that you made, this is not the
13 place to do this. ALICO is a life insurance company, your
14 Honor. The companies and the firms and associations do not
15 receive life insurance. The contracts are to people, human
16 beings. So that provision is not relevant. In fact, I'll just
17 offer this, proffer to the court. DFS never alleged that
18 provision was relevant. The only reason I raise it, again,
19 your Honor, was just to say that this is not the place to be
20 arguing these provisions.

21 The broader point we'd like to make, your Honor, is
22 really on the, apparently, the fourth amended complaint. We
23 actually heard the complaint being amended for the last couple
24 of hours as the court asked questions. And now it is
25 essentially a request to skip -- to ignore the third amended

F7M9USAA

1 complaint, ignore the second amended complaint, and now go to a
2 fourth amended complaint to try to address the issues that the
3 court has raised today. And Mr. Grabcheski, apparently, was
4 giving information to Mr. Goldfarb right in front of the court
5 to give some more specific facts, alleged facts about
6 conversations, meeting, things that occurred.

7 Your Honor, just to put this in context again.
8 Mr. Grabcheski filed an original complaint in May of 2010 in
9 which he raised a bunch of complaints, issues that the Southern
10 District of New York investigated. He raised a bunch of
11 alleged illegal behavior that AIG, ALICO, AIA engaged in.
12 You've heard today, you've seen in the multiple complaints, all
13 of these terrible things that AIG is alleged to have done --
14 AIG officials, executives, ALICO people -- fraudulent criminal
15 acts. Your Honor, he never said anything about those the first
16 time he went to the federal government. Not one thing.

17 Now, your Honor, the only reason I raise that, because
18 I think it's relevant to assessing the credibility of a
19 complaint and a relator who comes back to this court four times
20 and just today figures out well, I had a direct conversation
21 with this person, I'll put it on the record, that this person
22 told me that we were committing a fraudulent act to hide
23 activities from regulators.

24 Didn't remember that in May of 2010. No idea. And
25 that was four years ago. He had just been fired. The DRA had

F7M9USAA

1 just been signed. The world was collapsing around us. AIG was
2 going under. I didn't remember it then. But I remember it
3 today in court in 2015.

4 Your Honor, again, the only reason I raise that is
5 because the reason we have all of these rules about amending
6 complaints is partially so that we can understand the
7 credibility and assess the credibility of changes and
8 amendments to the complaint. And the fact that he never
9 mentioned them one time, one single time before today. And had
10 never mentioned the first time -- none of these issues, the
11 first time that he filed the complaint has to cast doubt on the
12 credibility of those claims.

13 I think that goes to the broader point that the fourth
14 amended complaint that is being proposed today is at least two
15 complaints too far and this case should stop at the second
16 amended complaint and should be dismissed with prejudice.

17 Just a few specific points on the -- Mr. Goldfarb's
18 claims about the specificity of knowledge and Mr. Grabcheski's
19 claims that people said things or he knew things. I want to
20 look at 104, paragraph 104. This was the paragraph that
21 Mr. Goldfarb says is all about the intent and him knowing that
22 people believed this and that people were telling him this and
23 were doing these things in order to evade the law and break the
24 law. Well what does it actually say, your Honor?

25 It says, "AIG engaged in a series of actions that were

F7M9USAA

1 designed to conceal the fact that GMD was soliciting and
2 selling insurance in New York on behalf of ALICO and AIA. As
3 described below, those activities included treating GMD's
4 New York sales force for payroll purposes at various times as
5 if they were employees of one or another of AIG subsidiaries,
6 other than ALICO or AIA. Even those employees regarding
7 themselves as employees of AIG were de facto employees of AIG."

8 Your Honor, there's nothing in that paragraph which
9 Mr. Goldfarb relied on that says anything about anybody's
10 intent, any conversations anyone had, anything anyone said to
11 anybody. These are conclusionary statements that
12 Mr. Grabcheski put into a complaint. Nothing at all about
13 anybody saying anything to him or to anyone about any of those
14 things.

15 Then the famous paragraph 107. And I'll read it more
16 slowly. Excuse me.

17 "On one or more occasions over the next few years,
18 AIG's chief financial officer, initially Howard Smith and
19 subsequently David Herzog, questioned the inclusion of the GMD
20 sales staff and payroll code 032 which increased expenses that
21 were charged to AIG as opposed to being charged to one of the
22 subsidiaries. In response, it was explained to them, either
23 directly or through a subordinate who reported the information
24 to them (a) that these employees were GMD New York employees
25 based in New York who serviced the multinational segment of

F7M9USAA

1 AIG's business primarily on behalf of ALICO; and (b) the
2 employees had been based in New York because of how many the
3 multinational clients and potential clients had offices in
4 New York; and (c) that the employees could not be put into
5 ALICO's payroll because ALICO was not licensed as an insurer in
6 New York because putting them on ALICO's payroll would
7 jeopardize the regulatory exemptions and tax breaks that ALICO
8 enjoyed under Delaware law which were not available to insurers
9 that transacted insurance in the United States."

10 Now, your Honor, once again, that paragraph contains
11 nothing about conversations that Mr. Grabcheski had, nothing
12 about where these came from, who said what to whom. There's a
13 lot of passive voice about it was told to people.

14 And most fundamentally about 107, and your Honor
15 touched on this, there's literally nothing in this paragraph
16 that remotely hints of illegal behavior. Everything that is
17 described in this paragraph is linked up to a payroll code,
18 your Honor, a payroll code at AIG, and where an employee should
19 be put on a payroll code. And apparently the motivation was
20 because ALICO's payroll, they were not licensed as an insurer
21 in New York, which was true. It was not illegal. They didn't
22 want to put these people on that because it would jeopardize
23 ALICO's lack of -- tax exemptions for not being licensed in
24 New York.

25 Your Honor there's nothing else in this paragraph --

F7M9USAA

1 there's nothing in this paragraph that says anything about what
2 is illegal about that. And there's certainly nothing on the
3 face of it that's illegal. And every single paragraph -- I
4 won't bore the court and waste more time -- but every single
5 paragraph in this complaint that Mr. Goldfarb pointed to as
6 evidence of intent, evidence of people having conversations
7 about criminal behavior, every one of them is like this.

8 And, again, Mr. Grabcheski never once, ever once said
9 in 2010, 2011, 2014 when he amended these complaints that any
10 of these conversations ever happened. He said it the first
11 time today to Mr. Goldfarb right in front of the court. That's
12 the first time. It's not even in his declarations that he
13 submitted in support of the third amended complaint.

14 Your Honor just a couple more points. Two more points
15 to make.

16 The Southern District of New York. And I sort of
17 think of this as a bit of a shuffle on the Southern District of
18 New York. And this goes to the original source issue which, of
19 course, follows from the public disclosure issues.

20 Mr. Goldfarb still refused to address the question of
21 what was the information that Mr. Grabcheski sourced to the
22 Southern District of New York in this investigation. He did
23 not answer it. It's not in the declarations. When he was up
24 here, he didn't address the point. All he would focus on was
25 the state authorities.

F7M9USAA

1 The Southern District of New York of course is the
2 operative federal government authority in this matter and
3 Mr. Goldfarb refused or did not address that point.

4 Again, it goes to the original fact, undisputed fact
5 in this case that the original complaint had nothing to do with
6 anything that's before the court now. The inference that
7 should be drawn from that is that Mr. Grabcheski told the U.S.
8 Attorney's Office nothing about what is in the case today.
9 Just not there. And the -- and again, we have to go beyond the
10 complaint for this but since we were doing that quite a bit
11 with Mr. Goldfarb I'll just offer up this point. The Southern
12 District issued subpoenas and the SIG TARP, the Special
13 Inspector General for the TARP program, issued subpoenas to AIG
14 in the summer of 2010 and investigated these issues. And those
15 subpoenas asked for information about ALICO's activities in the
16 United States, its marketing activity, which Mr. Grabcheski had
17 never mentioned in his original complaint. At the same time
18 that that complaint was filed, the U.S. Attorney's Office was
19 asking about something he never asked about. And then a year
20 later he puts it in a complaint which Mr. Goldfarb was very
21 careful to say he provided and disclosed to the U.S. Attorney's
22 Office but does not claim that he was the original source of
23 that information. And to the extent the original source issue
24 comes into play, I think it is abundantly clear on the record
25 that there is no basis to believe that Mr. Grabcheski was the

F7M9USAA

1 original source for the U.S. Attorney's Office for the Southern
2 District of New York. He may have been for DFS. He may have
3 been for the D.A.'s Office. He may have been for the New York
4 A.G.'S Office, but he wasn't for the Southern District of
5 New York.

6 Your Honor just one last point on materiality. The
7 issue with materiality here is something the court really
8 focused on and I think it is an important point.

9 AIG not only paid back all of the loan that was given
10 to it as part of the ALICO and AIA transactions. In fact, as
11 part of the overall structure, AIG paid the government \$20
12 billion or so more than the U.S. Government gave AIG. So the
13 U.S. government actually made a substantial amount of money off
14 of the entire loan profile.

15 So, the idea that materiality is not relevant -- and
16 it's not just about damages, your Honor. It's about the very
17 fundamental question of materiality. There is no allegation in
18 this case at all, and Mr. Goldfarb couldn't come up with one
19 today, about why this alleged a hundred million dollars which I
20 think was pretty clear is based on nothing at all remotely
21 relevant to this case, to the federal government case. How
22 that has any bearing on materiality, how that -- how you
23 establish it, how he would establish it, where that comes from,
24 other than these state law consent orders, is not described,
25 not explained, not addressed. It's simply there. And we're

F7M9USAA

1 supposed to then assume materiality, even though the facts, as
2 the court can take notice of, are that AIG paid everything back
3 and actually overall paid the government \$20 billion more than
4 they were loaned.

5 So at the end of the day, materiality -- it's not even
6 about the legal issues of materiality. It's about a
7 fundamental, again, Iqbal Twombly issue on materiality. There
8 is no allegation. There is no particularity. There is no
9 specificity. A number is made up out of thin air. A hundred
10 million dollars is a basis to claim that that's how much this
11 alleged violation of state law cost the federal government even
12 though the reality is, as we all know, the federal government
13 made money off of AIG.

14 Your Honor, unless you have any further questions, I'm
15 going to stop there.

16 THE COURT: No. Thank you very much.

17 MR. GOLDFARB: Your Honor, if I could just address a
18 few things.

19 First of all, I want to thank Mr. Burck for bringing
20 up the issue of communications with the U.S. Attorney's Office
21 because that was something I meant to bring up but was
22 distracted with the other issues and forgot to. And that is
23 that he is not correct that -- he said that the idea of these
24 claims was, of the U.S. Attorney's Office, there was something
25 that Mr. Grabcheski did disclose to the U.S. Attorney, and the

F7M9USAA

1 idea of the claim that we brought was an idea from
2 Mr. Grabcheski's counsel. So it was not a suggestion by the
3 U.S. Attorney's Office. And that's something that we can go
4 into if we have an opportunity to file another amended
5 complaint.

6 With regard to the issue of credibility.
7 Mr. Grabcheski isn't the one who drafted the complaints.
8 Counsel did that. We did it based on what we thought would be
9 a sufficient amount of information. Obviously, you can debate
10 whether what we did was sufficient. We think it was. They've
11 argued it wasn't. But that's certainly got nothing to do with
12 Mr. Grabcheski's credibility, even if credibility were
13 something that could be considered at this point.

14 Additionally, just with regard to the statute and the
15 language. And they said life insurance policies are given to
16 individuals. Well, the policies include also health insurance
17 policies. And the contracting people. It doesn't say
18 necessarily -- it says issuance or delivery of a policy or
19 contract of insurance.

20 A group health insurance policy, that's issued and
21 delivered to the employer. The individual employees are
22 covered insureds. But that language certainly is broad enough
23 to cover that. So that doesn't really prove anything.

24 Other than that I think I've said what I've had to
25 say. I think the Court should allow one more opportunity to

F7M9USAA

1 amend and give us that shot. Thank you.

2 THE COURT: Let me look and see if I think that that
3 is appropriate or necessary or futile.

4 Let me go back to the papers. I want to get this
5 transcript because this is helpful to me, given the volume of
6 paper there, but I'm going to try to see if I can try to
7 resolve fairly quickly in the next 30 or 60 days. Thank you
8 very much.

9 (Adjourned)

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